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HAROLD B. WILLEY,

No. 280

Supreme Court of the United States

OCTOBER TERM, 1953

PHILLIPS PETROLEUM COMPANY, *Petitioner*,

v.

STATE OF WISCONSIN AND PUBLIC SERVICE COMMISSION OF WISCONSIN, CITY OF DETROIT, MICHIGAN, CITY OF KANSAS CITY, MISSOURI, CITY OF MILWAUKEE, a municipal corporation, COUNTY OF WAYNE, MICHIGAN, and THE FEDERAL POWER COMMISSION, *Respondents*

BRIEF FOR PETITIONER PHILLIPS PETROLEUM COMPANY

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INDEX

	Page
Opinions Below	1
Jurisdiction	2
Question Presented	2
Statute Involved	2
Statement	3
I. The Proceedings Before the Federal Power Commission	3
A. The Parties and Hearings before the Commission	3
B. The Facts	4
C. The Opinion and Findings of the Commission	10
II. The Proceedings in the Court Below	11
Specification of Errors to be Urged	12
Summary of Argument	13
Argument	18
I. The Natural Gas Act Excludes from Federal Regulation the Whole of the Business of Production and Gathering, Including Sales for Resale in Interstate Commerce Made as a Part of that Business	18
A. The Natural Gas Act on its Face Regulates only Companies Performing the Interstate Service of Transporting Gas from the Producing Fields to Consumer Markets and Excludes from Federal Regulation the Whole of the Business of Producing and Gathering	19
B. The Legislative History of the Natural Gas Act Shows that Congress Intended to Regulate the Interstate Transmission Companies and that it Did Not Intend to Regulate Independent Producers or Gatherers	27
1. The Federal Trade Commission Report	27

Page

2. The Committee Hearings and Reports... 30

3. The Debates 41

C. The Federal Power Commission's Consistent Administration of the Natural Gas Act Confirms the Absence of Commission Jurisdiction over the Business of Independent Producers and Gatherers, Including Sales by Them for Resale 45

D. The Decisions of this Court Recognize that the Natural Gas Act Does Not Authorize any Direct Federal Regulation of the Business of Producing and Gathering 49

II. The Decision of the Federal Power Commission that Phillips' Sales Are Not Subject to Federal Regulation Because They Are Part of the Business of Producing and Gathering Is Correct in Law and Fact and Should Be Upheld 58

A. The Commission Correctly Construed the Natural Gas Act to Exclude the Whole of the Business of Producing and Gathering 58

B. The Commission Correctly Found that Phillips' Movement, Processing and Sales of Natural Gas Are All a Part of the Business of Producing and Gathering 67

III. The Decision of the Federal Power Commission that Sales Such as Those of Phillips Are Not Subject to Federal Regulation Is Confirmed by Its Finding That Its Regulation of Such Sales Would Be Inconsistent With State Conservation Programs 73

IV. The Assertion that Extension of Federal Regulatory Power to the Activities of Independent Producers and Gatherers Is Required to Protect Consumers Is Without Basis in Fact and in Any Event Raises Questions of Legislative Policy That May Appropriately be Considered Only by Congress 85

Conclusion 94

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CITATIONS

CASES: Page

American Sugar Refining Co. v. Louisiana, 179 U. S. 89 25
Bandini Petroleum Co. v. Superior Court, Los Angeles County, Calif., 284 U.S. 8 40
Bethlehem Steel Co. v. New York State Labor Relations Board, 330 U.S. 767 83
Billings Gas Co., 2 F.P.C. 288 .....47, 49
Brown v. Maryland, 12 Wheat. 419 25
Cardillo v. Liberty Mutual Co., 330 U.S. 469 70
Carter v. Liquid Carbonic Pacific Corporation, 97 F. 2d 1 (9th Cir. 1938) 69
Cities Service Gas Co. v. Peerless Oil & Gas Co., 340 U.S. 179 .....41, 51, 56, 61, 62, 63, 64, 65, 66, 67, 71, 79, 86
Cloverleaf Butter Co. v. Patterson, 315 U.S. 148 ... 83
Colorado Interstate Gas Co. v. Federal Power Commission, 324 U.S. 581 .....16, 49, 50, 51, 53, 55, 56, 57, 58
Columbian Fuel Corporation, 2 F.P.C. 200....15, 45, 46, 47, 48, 49, 92, 93
Cooley v. Board of Wardens of the Port of Philadelphia, 12 How. 298 41
Federal Power Commission v. East Ohio Gas Co., 338 U.S. 464 .....30, 35, 63, 64, 71
Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591 .....16, 30, 40, 49, 50, 51, 52, 53, 55, 89
Federal Power Commission v. Natural Gas Pipeline Co., 315 U.S. 575 50
Federal Power Commission v. Panhandle Eastern Pipe Line Co., 337 U.S. 498 .....16, 24, 30, 34, 40, 42, 48, 57, 58, 61
Federal Trade Commission v. Bunte Brothers, Inc., 312 U.S. 349 48
The Fin-Ker Oil and Gas Production Co., 6 F.P.C. 92 47
Freeman v. Hewit, 329 U.S. 249 64
Gray v. Powell, 314 U.S. 402 .....70, 73
Hassie Hunt Trust, 6 F.P.C. 835 48
Henderson Co. v. Thompson, 300 U.S. 258 40
Interstate Natural Gas Co. v. Federal Power Commission, 331 U.S. 682 .....16, 26, 49, 53, 54, 55, 56, 62, 74

	Page
Interstate Natural Gas Co., Inc., 3 F.P.C. 416	48, 54
Kansas-Nebraska Natural Gas Co., Inc., 6 F.P.C. 664	47
La Gloria Corp., 7 F.P.C. 349	48
Levinson v. Spector Motor Service, 330 U.S. 649	48
Lindsley v. Natural Carbonic Gas Co., 220 U.S. 61	40
Michigan-Wisconsin Pipe Line Co. v. Calvert, Nos. 198-201, Oct. Term 1953 (22 U.S. Law Week 4115, February 8, 1954)	64, 65
Missouri v. Kansas Natural Gas Co., 265 U.S. 298	38, 39
National Labor Relations Board v. Hearst Publications, Inc., 322 U.S. 111	48, 70
Northern Natural Gas Company, Docket No. G-1618, 94 P.U.R. (NS) 485 (1952)	91
Northern Natural Gas Company, et al. v. Federal Power Commission, Nos. 381 and 382, Supreme Court of the United States, Oct. Term 1953	50
Norwegian Nitrogen Products Co. v. United States, 288 U.S. 294	48
O'Hara v. Luckenbach S.S. Co., 269 U.S. 364	22, 69
Ohio Oil Company v. Indiana (No. 1), 177 U.S. 190	40
Order of Railway Conductors v. Swan, 329 U.S. 520	22, 69
Palmer Oil Corp. v. Amerada Corp., 343 U.S. 390	77
Panhandle Eastern Pipe Line Co. v. Public Service Commission of Indiana, 332 U.S. 507	40, 52
Phillips Petroleum Co. v. Oklahoma, 340 U.S. 190	66
Pierce Oil Corp. v. Phoenix Refining Company, 259 U.S. 125	40
The Pipe Line Cases, 234 U.S. 548	25
Prudential Insurance Co. v. Benjamin, 328 U.S. 408	63
Public Utilities Commission v. Attleboro Steam & Electric Co., 273 U.S. 83	38, 39
Repollo Oil Co., 2 F.P.C. 1004	47
Roberts v. Tennessee Coal, Iron & R. Co., 255 Fed. 469 (5th Cir. 1919), cert. den. 250 U.S. 659	69
Sinclair Prairie Oil Co., 2 F.P.C. 1009	47
Sinclair Prairie Oil Co., 6 F.P.C. 1059	48
South Carolina State Highway Department v. Barnwell Brothers, Inc., 303 U.S. 177	41
The Superior Oil Co., 7 F.P.C. 627	48
Tennessee Gas and Transportation Company and The Chicago Corporation, 6 F.P.C. 98	47

Page

United States v. American Trucking Ass'ns, Inc., 310 U.S. 534 48
United States v. Chicago North Shore & Milwaukee R. Co., 288 U.S. 1 48
United States v. Maher, 307 U.S. 148 .....22, 69
United States v. Public Utilities Commission of California, 345 U.S. 295 52
United States v. Wabash R. Co., 321 U.S. 403 70
Unemployment Compensation Commission of Alaska v. Aragon, 329 U.S. 143 70
Walls v. Midland Carbon Co., 254 U.S. 300 40
R. J. and D. E. Whelan, 6 F.P.C. 672 48
Willson v. Black-bird Creek Marsh Co., 2 Pet. 245.. 41

FEDERAL LEGISLATION:

Natural Gas Act of June 21, 1938, ch. 556, 52 Stat. 821, as amended by Act of February 7, 1942, ch. 49, 56 Stat. 83, and Act of July 25, 1947, ch. 333, 61 Stat. 459, 15 U.S.C. §§ 717 *et seq.* 2, 11, 13, 14, 21, 22, 23, 24, 25, 26, 27, 45, 59, 61, 70

FEDERAL LEGISLATIVE DOCUMENTS:

S. Res. 83, 70th Cong., 1st Sess. 28
Final Report of the Federal Trade Commission to the Senate of the United States pursuant to Senate Resolution No. 83, 70th Cong., 1st Sess., Part 84-A (Senate Document 92, 76th Cong., 1st Sess.) (1935) 4, 19, 20, 27, 28, 29, 72
S. J. Res. 115, 73rd Cong., 2d Sess. 28
Hearings on H.R. 11662, 74th Cong., 2d Sess...30, 31, 32, 33, 34, 35
H. R. 12680, 74th Cong., 2d Sess. 30, 35
Hearings on H.R. 4008, 75th Cong., 1st Sess....30, 32, 33, 34, 35, 38
H. R. 6586, 75th Cong., 1st Sess. 30, 35, 42
H. Rep. 709, 75th Cong., 1st Sess. 35, 36, 37, 38
Cong. Rec. Vol. 81 .....42, 43, 44, 45
Cong. Rec. Vol. 83 41
Hearings before Committee on Interstate and Foreign Commerce on H.R. 2185, 80th Cong., 1st Sess. (1947) 89

Page

Hearings before Subcommittee of the Committee on Interstate and Foreign Commerce on S. 734, 80th Cong., 1st Sess. (1947) 89
Hearings before Subcommittee of the Committee on Interstate and Foreign Commerce on H.R. 79, 81st Cong., 1st Sess. (1949) 89, 90
Hearings before Subcommittee of the Committee on Interstate and Foreign Commerce on S. 1498, 81st Cong., 1st Sess. (1949) 90

STATE STATUTES, REGULATIONS AND ORDERS:

New Mexico Oil Conservation Commission Rule 507 77
New Mexico Stat. (1951 Supp.), §§ 69-212, 213, 213½, 213½(e), 214b, 8-1138, 1139 .....77, 79, 81
Oklahoma Corporation Commission Order No. 26906, August 8, 1952 .....66, 67
Oklahoma Stat., Tit. 52, §§ 239, 287.1-287.15 (1951)..77, 81
Vernon's Civil Stat. of Texas (1925, as amended), Art. 6008, §§ 10-20, Art. 6008a, Art. 6008b, § 1, Art. 6009, § 20, Art. 6049a, §§ 8, 8a, 8aa, 8b, Art. 6049d, §§ 4-13 .....77, 79, 81

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Brief for Federal Power Commission, Interstate Natural Gas Company v. Federal Power Commission, No. 733 (Oct. Term 1946) 55
DeVane, Highlights of Legislative History of the Federal Power Act of 1935 and the Natural Gas Act of 1938, 14 Geo. Wash. L. Rev. 30 (1945)....31, 46
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Mineral Market Report, No. MMS 2229, Mineral Industry Surveys, United States Department of Interior, Bureau of Mines, November 9, 1953 88
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Page

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Note, 52 Col. L. Rev. 135 (1952) 45
Note, 22 Geo. Wash. L. Rev. 118 (1953) 45

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BRIEF FOR PETITIONER PHILLIPS PETROLEUM COMPANY

OPINIONS BELOW

The opinion of the Court of Appeals for the District of Columbia Circuit (R. 1842-1856) is reported at 205 F. 2d 706. The opinion, findings and order of the Federal Power Commission (R. 1682-1753) are reported at 10 F.P.C. 246.

JURISDICTION

The judgment of the Court of Appeals was entered May 22, 1953 (R. 1858). The petition for a writ of certiorari was filed on August 20, 1953 and denied by this Court on November 30, 1953. A petition for rehearing was filed on December 14, 1953. On January 18, 1954, this Court granted the petition for rehearing, vacated the order denying certiorari, and granted the petition for certiorari.

The jurisdiction of this Court rests upon 15 U.S.C. Section 717r(b) and 28 U.S.C. Section 1254(1).

QUESTION PRESENTED

Petitioner, Phillips Petroleum Company, produces natural gas and gathers this gas, together with gas it purchases from other producers, by networks of pipe lines located in the producing field. The gas moves from the wells through these pipe lines to a plant or plants, located in the field, where gas from different lines serving different parts of the field is commingled; as the gas moves through the plant liquid hydrocarbons and impurities are removed. A part of the residue gas is used or sold locally, and the remainder is delivered at outlets of the plants to pipe line companies which transport it interstate and resell the gas for use in consumer markets. All of these activities are carried on by Phillips in the producing fields; Phillips does not own or operate an interstate transmission line, *i.e.*, a pipe line transporting gas interstate between the producing fields and markets, and it is not affiliated with any company that owns or operates such a line.

The question presented is whether the Federal Power Commission was correct in determining that Phillips' sales to the interstate pipe line companies are not subject to regulation under the Natural Gas Act.

STATUTE INVOLVED

The pertinent provisions of the Natural Gas Act (Act of June 21, 1938, ch. 556, 52 Stat. 821, as amended, 15 U.S.C. 717 *et seq.*) are set forth in Appendix A.

STATEMENT

I. The Proceedings Before the Federal Power Commission

A. The Parties and Hearings Before the Commission

By an order dated October 28, 1948 the Federal Power Commission instituted an investigation to determine (1) whether Phillips was a natural gas company within the meaning of the Natural Gas Act and if so, (2) whether any of its rates were unjust or unreasonable (R. 1647-1660). On April 17, 1951, the Commission limited the investigation to the first question and postponed consideration of the second until a later date (R. 1676).

The State of Wisconsin and its Public Service Commission, the City of Kansas City, Missouri, the City of Milwaukee, the City of Detroit, Michigan, the County of Wayne, Michigan, and the Michigan Public Service Commission intervened in the proceeding, contending that Phillips was a natural gas company and that its sales should be regulated by the Federal Power Commission (R. 5-6, 1687).

The producing States of New Mexico, Oklahoma, and Texas (petitioners in No. 281) intervened, contending that Phillips' sales were not subject to regulation under the Natural Gas Act because regulation of those sales by the Federal Power Commission would interfere with the exercise of the regulatory functions of the states (R. 80-83, 87-93, 100-103). The three States participated in the hearings before the Commission and presented extensive evidence in support of their position, including testimony from members of their regulatory agencies. The producing States of Arkansas, Kansas, Louisiana and Mississippi also intervened in opposition to federal regulation of Phillips' sales (R. 6, 1686-1687), but evidence offered by these States was excluded by the examiner on the ground

that no gas produced within these States was involved in the proceeding.[1]

Hearings were held before an examiner from April 3, 1951, to May 23, 1951. The record made before the examiner consisted of nearly 11,000 pages, including approximately 5,800 pages of testimony and nearly 4,000 pages of exhibits.

B. The Facts

On the record presented to the Commission, the facts relating to Phillips' operations may be summarized as follows:

Phillips is an integrated oil company, which is also engaged in the production, gathering and sale of natural gas (Ex. 29; R. 862-871, 1687-1689). All of Phillips' gas operations are carried on in the producing fields (Ex. 82; R. 1215). Phillips is an "independent" producer and gatherer of gas, that is to say, it does not own or operate an interstate transmission system by which gas is moved from the fields to consumer markets, and it is not affiliated with any company that owns such a system.[2]

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[1] The Independent Natural Gas Association of America, Old Ocean Royalty Owners Association, Texas County Land and Royalty Owners Association, and Texas Independent Producers and Royalty Owners Association also intervened, and took the position that under the Natural Gas Act sales such as those made by Phillips are not subject to federal regulation (R. 6, 1687).

[2] The word "independent" has long been used in the industry and by commentators to denote the difference between producers and gatherers who do nothing but produce, gather, process and sell in the gas fields, on the one hand, and interstate transmission companies which produce, gather and transport by pipe line to consumer markets, on the other. Final Report of the Federal Trade Commission to the Senate of the United States, pursuant to Senate Resolution No. 83, 70th Cong., 1st Sess., Part 84-A (Senate Document 92, 70th Cong., 1st Sess.), p. 479 (1935); Natural Gas Investigation, Federal Power Commission, Docket No. G-580, Report of Commissioners Smith and Wimberly, (United States Government Printing Office 1948), pp. 156, 164, 171, 172, 173-174; Berger and Krash, Status of Independent Producers under the Natural Gas Act, 30 Tex. L. Rev., p. 29, n. 1 (1951).

As of December 31, 1949 Phillips owned or controlled by contract 15.22 trillion cubic feet of proven gas reserves (R. 1689). It also owns gathering lines and processing plants, located in the oil and gas fields, which are used by Phillips both in the conduct of its gas business and in various aspects of its petroleum business (R. 1689).[3] In 1949 Phillips sold approximately 400,000,000 m.c.f. of natural gas and in 1950 approximately 500,000,000 m.c.f. (R. 1689). Between 50% and 60% of the natural gas sold by Phillips is sold to interstate pipe line companies which transport the gas from the producing fields to consumer markets (R. 1689). Phillips' gas operations, although extensive, are over-shadowed by its operations in the petroleum and chemical industries; in 1949 Phillips' gas operations accounted for only 4.2% of its total gross operating revenues (Ex. 29; R. 852).

The bulk of the evidence taken by the examiner related to Phillips' production, gathering and sales of natural gas in the producing fields of Oklahoma, Texas and New Mexico. The sales involved are made to five interstate transmission companies: Michigan-Wisconsin Pipe Line Company, Panhandle Eastern Pipe Line Company, Independent Natural Gas Company, El Paso Natural Gas Company, and Cities Service Gas Company (R. 1690-1711). Each of these companies owns and operates an interstate pipe line and is admittedly a natural gas company within the meaning of the Natural Gas Act (R. 1827-1834). The gas involved in these transactions includes gas that is produced by Phillips and gas that it buys from other producers. All of the gas is gathered by Phillips.

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[3] Natural gas liquids as well as natural gas prepared for delivery to pipe line companies for transportation to consumer markets are products of every processing plant operated by Phillips which is involved in this case (Exs. 169-177; R. 630, 1329, 1359, 1389, 1421, 1455, 1513, 1573, 1609, 1639).

Gas is delivered by Phillips to these five companies from separate gathering systems. Altogether there are nine gathering systems, including twelve different processing plants, involved in the transactions between Phillips and the five companies (R. 1691-1710).[4] Five of the gathering systems are located entirely in Texas, one entirely in Oklahoma and one entirely in New Mexico (Exs. 14B-15A, 48-51; R. 816-819, 896-903, 1697, 1699, 1703, 1705, 1710); in the case of the other two gathering systems the processing plants are located in Texas but serve the Hugoton Field that extends into both Texas and Oklahoma; hence the gathering lines for those plants lie in both states (Exs. 12A-13A; R. 810-813, 1691, 1695).

The various gathering systems differ in location, size and physical characteristics, but they all have certain features in common: In each case the gathering system includes a network of converging pipe lines and a processing plant or plants (Exs. 12A-15A, 48-51, 86, 91, 103, 104, 111, 116; R. 810-819, 896-903, 1215, 1224, 1239, 1244). In each case the gas, both that produced by Phillips and that which Phillips buys from others and gathers, moves from the wells through the gathering lines to a processing plant located at some central or convenient point in the field (R.

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[4] The processing plants are: Sherman, Hansford, Dumas, Sneed, Gray, Eunice, Goldsmith, Crane, Fullerton, Edmond, Hunton and Trindle. The first eight of these plants are owned and operated by Phillips. The Fullerton plant is owned by Phillips and the Fullerton Oil Company, an independent producer and gatherer. The Edmond plant is owned by Phillips and Continental Oil Company, another independent producer and gatherer of natural gas, and is operated by Phillips (Ex. 52; R. 287, 1030). The Hunton plant is owned by Phillips and five other independent producers and gatherers of natural gas (R. 1710). The Trindle plant is owned and operated by the West Edmond Hunton Lime Unit, a unitized operation set up pursuant to Oklahoma law (Ex. 52; R. 287, 289, 905-966).

The Sneed and Dumas plants are part of a single gathering system; the Edmond, Hunton and Trindle plants are similarly parts of a single gathering system.

1743).[5] The lines vary in size, in many instances being of small diameter (3 to 6 inches). As the lines approach the processing plants and gas from additional wells enters the lines they tend to increase in size; the lines leading into the plants range from 12 to 26 inches in diameter. More than 75% of the total mileage of pipe involved consists of pipe of a diameter of 12 inches or less (Exs. 12A-15A, 48-51, 86, 91, 103, 104, 111, 116; R. 810-819, 896-903, 1215, 1224, 1239, 1244). More than one line serves each of the processing plants involved, and the final commingling of gas from the different lines occurs in each case in the processing plant (Exs. 45A-45-H-I; R. 872-895, 1743).[6]

The processing which occurs within the plants consists in the extraction of liquid hydrocarbons and in the removal of hydrogen sulphide or other impurities (R. 1742-1743).

Approximately half of the gas gathered by Phillips is casinghead gas, that is, gas produced from oil wells in conjunction with oil (Exs. 169-177; R. 282-284, 291, 1298-1639). The oil cannot be produced without the gas which

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[5] The distances that the gas moves through the gathering lines are relatively short. Variations in the length of the movements depend upon the distance of the wells from the processing plants, ranging from less than a quarter of a mile to a maximum of 45 miles. All movements are within the confines of the field in which the gas is produced (Exs. 12A-15A, 48-51, 86, 91, 103, 104, 111, 116; R. 810-819, 896-903, 1215, 1224, 1239, 1244).

[6] For example, the six lines which gather gas at the Hansford plant come together from the north and south, east and west and northeast and northwest (Ex. 13A; R. 813). Similarly, six lines, from the north, west and south, carry gas into the Goldsmith plant (Ex. 50; R. 901). See plats attached as Appendices B and C.

In some of the gathering systems the pattern of movement of the gas will vary substantially from time to time. The gas at different points in the system may flow in different directions at different times because of the location of the plants receiving gas from the system, the open loops within the system and the variation in the wells and lines operating or shut in from time to time (R. 142-146, 149-150).

must be gathered and prepared for market if it is not to be flared or otherwise wasted.

Much of the casinghead gas is not produced by Phillips but is purchased by it from other independent producers under contracts which provide that the price paid by Phillips shall depend in part upon the gasoline content of the gas and in part upon the price which Phillips receives from the sale of residue gas (Exs. 62, 107, 124, 181-184; R. 361-363, 1164, 1283-1284, 1640-1644).[7] The contracts also require Phillips to return residue gas to these producers for use in their operations (R. 362). Phillips, accordingly, returns a portion of the residue to the independent producers from whom the casinghead gas was purchased, retaining for its own use or sale that part of the gas not required by these independent producers for their operations. Some of the gas so retained by Phillips is used in its own operations, some is sold to others for local use, but the greater part of this residue gas is delivered to the five interstate pipe line companies (Exs. 169-177, 181-184; R. 1298-1644).

In the case of each sale the gas is delivered by Phillips to the interstate pipe line company at the outlet or exhaust of the processing plant (Exs. 99A-102, 113, 114A, 117A; R. 1217-1223, 1240, 1245, 1691-1711, 1743-1744).[8] The outlet or

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[7] The same price relationship exists with respect to the gas produced by Phillips from leased acreage in the Hugoton Field. The royalty agreements provide that the royalty paid by Phillips shall depend in part upon the price which Phillips receives from the sale of the gas (Ex. 109B; R. 1224-1229).

[8] In two instances, the sales to Panhandle at the Sneed plant and those to El Paso at the Goldsmith plant, the raw gas is sold and delivered to the interstate transmission company at the plant line, subject to Phillips' right to extract and retain the liquid hydrocarbons in the gas. In these instances, the gas is compressed by the interstate transmission company, which retains title and redelivers the gas to Phillips for the extraction process, and is then in turn redelivered to the transmission company (Exs. 45B, 45G-1; R. 129, 206-209, 213-214, 253-255, 875, 891). In the case of the sale to Panhandle the gas delivered by Phillips is commingled by Panhandle with other gas before being returned for processing (Ex. 14B; R. 817).

exhaust is a pipe that carries the gas to a point within, or at the border of, the plant yard where the gas enters a pipe line owned and operated by the interstate transmission company which is purchasing the gas. The length of these plant exhausts or outlets varies from approximately 200 to 1490 feet (Ex. 192; R. 1646). In no case does Phillips perform any operation with respect to the gas beyond the plant yard. The transmission companies transport the gas in interstate commerce from the producing fields and resell it either at city gates or at other points for ultimate consumption in consumer markets located in Arizona, California, Illinois, Indiana, Iowa, Kansas, Michigan, Minnesota, Missouri, Nebraska, Ohio and Wisconsin (R. 1827-1834).

The sales to Cities Service differ from those to the other four transmission companies in that the gas involved is not all owned by Phillips but is produced from an oil field unitized by order of the Oklahoma Corporation Commission (Ex. 52; R. 905-1051). Each unit owner has an undivided interest in the residue gas. As a unit owner Phillips has an undivided 19.6% interest in the unit production of oil and gas (Ex. 52; R. 281-282, 1048). There are approximately 52 other independent producers who have interests in the unit (R. 910).[9] Sales of the gas are made for all of the unit owners from the Edmond, Hunton and Trindle (North) plants (R. 287). Phillips as agent for all the unit owners, collects from Cities Service the proceeds of the sales at the three plants and disburses the proceeds to the various unit owners in proportion to the gas sold (R. 281-282, 289, 291).

Plats of Phillips' Goldsmith and Hansford gathering systems, two of the nine systems involved in this case, marked Appendices B and C respectively, are at-

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[9] The royalty interests under the leases in this unit are owned by approximately 2500 royalty owners; the royalty payments made to these owners depend in part upon the price received by the unit for the gas.

tached hereto.[10] These plats illustrate many of the aspects of the gathering systems that have been referred to in the preceding description. The Goldsmith plat, for example, shows Phillips' gathering lines by which gas is collected in the Goldsmith plant, residue lines through which Phillips returns gas to producers from whom it purchases casinghead gas, the interstate transmission line of El Paso Natural Gas Company, into which Phillips delivers gas at the Goldsmith plant (one of the deliveries involved in this case), and another line, owned by Sid Richardson, through which gas moves from the Goldsmith plant to a local plant, also owned by Richardson, where the gas is used in the manufacture of carbon black.[11]

C. The Opinion and Findings of the Commission

At the conclusion of the hearings before the examiner, the record was certified to the Commission which heard argument on July 9 and 10, 1951 (R. 1686).

In an opinion issued on August 22, 1951, the Commission held "that Congress, by the exemption of producing and gathering, intended to deny this Commission jurisdiction over the business of producing and gathering" (R. 1741).

On the basis of the whole record, including the facts that have been summarized above, the Commission found that Phillips' movement, processing and sales of natural gas are a part of Phillips' gathering business, or at least exempt under Section 1(b) of the statute as an incident of, or activity related, to its gathering business (R. 1742-1744, 1752-1753). The Commission also found that Phillips' sales were made during the course of production and gathering

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[10] The Goldsmith plat is based on Exhibit 91 (R. 1215) and Exhibit 50 (R. 901). The Hansford plat is based on Exhibit 13A (R. 813).

[11] The Hansford plat shows a gathering system (with lines that lie in both Texas and Oklahoma) that is used to collect dry gas; hence there are no lines for the return of residue gas similar to those shown on the Goldsmith plat.

and that regulation of those sales by the Federal Power Commission would be inconsistent with or would substantially interfere with the state regulation by New Mexico, Oklahoma and Texas (R. 1745-1747, 1753-1755).

On the basis of these findings the Commission held that Phillips was not a natural gas company within the meaning of the statute and ordered the proceeding terminated (R. 1753). One member of the Commission concurred on the second ground alone, *i.e.*, that federal regulation would be inconsistent with or would substantially interfere with state regulation, and one member dissented (R. 1753-1822).

II. The Proceedings In The Court Below

The State of Wisconsin and its Public Service Commission, the City of Kansas City, Missouri, the City of Milwaukee, the City of Detroit, Michigan, and the County of Wayne, Michigan, brought five separate proceedings in the United States Court of Appeals for the District of Columbia Circuit, pursuant to Section 19(b) of the Natural Gas Act, to review and to set aside the Commission's order (R. 1-72). Phillips and the States of New Mexico, Oklahoma and Texas intervened in each of these proceedings in support of the Commission's order (R. 72-117). The Commission appeared in each proceeding in defense of its order. The five petitions were consolidated for hearing by an order of the Court of Appeals dated February 5, 1952 (R. 1838-1839).

On May 22, 1953 the Court of Appeals in an opinion written by Judge Edgerton and concurred in by Judge Prettyman, with Judge Clark dissenting, set aside the Commission's order. The majority opinion stated that Phillips' sales were made "after the time and beyond the place at which production and gathering are complete and after processing has intervened" (R. 1842) and that the words "production or gathering" in Section 1(b) of the Act do not exempt "sales made after production and gathering have been completed" (R. 1849). The majority opinion also

stated that when Congress passed the statute it intended to subject to federal regulation all sales that could not be regulated by the states; that Phillips' sales are sales in interstate commerce of natural gas for resale and "it follows that no state can regulate these sales"; that Phillips' sales "are made after the gas has been gathered into trunk lines" and for that reason are not subject to state regulatory authority (R. 1847). The majority opinion does not make clear which of these several considerations it regarded as decisive. The concluding paragraph of the majority opinion reads as follows (R. 1849-1850):

> "Phillips urges that the Commission's findings are supported by substantial evidence and should therefore be sustained. But the validity or invalidity of the Commission's conclusion that Phillips is not a 'natural-gas company' does not turn upon the evaluation of testimony or upon any facts peculiar to this case. It turns upon the generic question whether the exemption of 'production or gathering' in § 1(b) of the Natural Gas Act covers interstate sales of gas by the corporation that produced and gathered it. We think the Act and the decisions of the Supreme Court permit only one answer. We think the Commission has applied an erroneous rule of law. Phillips' sales to the pipeline companies are not within either the statutory phrase 'the production or gathering of natural gas' or the Supreme Court's paraphrase 'made during the course of production and gathering'. Therefore Phillips is a 'natural-gas company' within the meaning of the Natural Gas Act and the Commission should fix the rates at which these sales are made."

SPECIFICATION OF ERRORS TO BE URGED

The Court of Appeals erred—

(1) In reversing the order of the Federal Power Commission and in holding that Phillips is a "natural-gas company" within the meaning of the Natural Gas Act and that its sales involved in this proceeding are subject to federal regulation.

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(2) In failing to hold that Section 1(b) of the Natural Gas Act excludes from federal regulation the whole of the business of production and gathering, including sales in interstate commerce for resale made as a part of that business.

(3) In rejecting findings made by the Federal Power Commission that all of Phillips' operations, including its movement, processing and sales of gas, are part of production and gathering.

(4) In concluding that Phillips' sales are made after the time and beyond the place at which production and gathering are complete.

(5) In concluding that in the exercise of their conservation powers the states cannot regulate Phillips' sales that are involved in this proceeding.

(6) In failing to give effect to findings by the Federal Power Commission that its regulation of Phillips' sales would be inconsistent with state regulatory programs.

SUMMARY OF ARGUMENT

I

There are three different businesses or economic functions involved in the operation of supplying natural gas to consumers. The first is the production and gathering of natural gas in the field. The second is the interstate transmission of the gas by pipe line from the producing fields to consumer markets. The third is the local distribution of the gas to the consumer markets. Phillips and other independent producers and gatherers are engaged solely in the first of these businesses. Their activities, which are confined to the producing fields, consist of producing gas, collecting it at some central point in the field and there preparing the gas for use or sale by removing impurities and liquid hydrocarbons. This is a business of predominantly local character which must be carried on within the

limits of detailed regulations imposed by the states in the exercise of their constitutional power to protect and conserve a wasting natural resource.

The sales of Phillips to the interstate transmission companies that are involved in this case are sales made by Phillips as a part of its business of producing and gathering. The Natural Gas Act does not authorize federal regulation of such sales.

In 1935 the Federal Trade Commission, following an extensive investigation made at the request of Congress, submitted a 600-page report on the activities of public utility corporations and holding company systems in the gas industry. The report was directed to the necessity for regulation of the practices of the interstate transmission companies which were engaged in the middle segment of the industry, that is, in the transmission of gas by pipe line from the producing fields to consumer markets. The report pictured those companies as occupying a dominant and monopolistic position in the industry.

As Section 1(a) of the Natural Gas Act shows, the statute was enacted in response to the disclosures made in this report. It was designed to regulate solely the activities of these transmission companies which transport gas from the producing fields to consumer markets. It was in no way intended to apply to the business of independent producers or gatherers or to regulate the prices at which they sell gas in the field to the transmission companies.

The intention to confine the regulation to the business of the interstate transmission companies and to exclude the business of producing and gathering from regulation is apparent on the face of the statute. Section 1(a) of the Act describes the business that is to be regulated and does so in terms that are applicable to the interstate transmission business and not to the business of producing and gathering. The concluding clause of Section 1(b) expressly excludes "production or gathering" from regulation and

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those words comprehend the whole of the business of independent producers and gatherers, including sales for resale in interstate commerce. The statutory purpose to regulate only the business of the interstate transmission companies is evidenced by the regulatory provisions of the statute. Those provisions authorize regulation of the kind historically applied to transportation services and similar public utilities. That regulation is appropriate to the business of the interstate transmission companies but would be unsuitable and inappropriate to regulation of the business of producing and gathering.

The legislative history, beginning with the Federal Trade Commission Report and ending with the debates in both Houses of Congress, where the bill was described as noncontroversial, sharply delineates the coverage of the Act. In the opening hearings on the legislation it was firmly established that federal regulation would not apply to the gathering business or prices paid in the field. Throughout the Congressional proceedings, emphasis was placed on the need to exercise control over the interstate transmission companies. A review of the entire legislative history demonstrates that Congress intended to regulate the activities of those companies, particularly their sales at the city gates, which could not be reached by the states, but that it did not intend to regulate the business of producing and gathering.

In enforcing the statute the Federal Power Commission has consistently given effect to this statutory purpose. Beginning with *Columbian Fuel Corp.*, 2 F. P. C. 200, decided in 1940, two years after the passage of the Act, the Commission has disclaimed authority to regulate the field prices of independent producers and gatherers. In the instant proceeding the Commission, after an extensive review of the history and provisions of the Act, reaffirmed this consistent interpretation of the Act.

The decisions of this Court interpreting and applying the provisions of the Natural Gas Act also reflect the stat-

utory scheme disclosed by the legislative history. Those decisions recognize that the Act was directed at the practices of the interstate transmission companies and that its provisions do not permit any direct regulation of production or gathering because that activity relates to problems that are primarily of local concern. *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591; *Colorado Interstate Gas Co.* v. *Federal Power Commission*, 324 U.S. 581; *Federal Power Commission* v. *Panhandle Eastern Pipe Line Co.*, 337 U.S. 498. In *Interstate Natural Gas Co.* v. *Federal Power Commission*, 331 U.S. 682, this Court stated that the statute did not permit federal regulation of sales for resale in interstate commerce even when made by an interstate transmission company if regulation of those sales would interfere with state regulatory authority. Any regulation of sales made by an independent producer or gatherer would, because of the nature of his business, necessarily and inevitably conflict with state regulatory authority. It follows under the *Interstate* case that such sales are not subject to federal regulation.

II

The determination by the Federal Power Commission that Phillips' sales are not subject to regulation under the Natural Gas Act is correct and should be upheld. The Commission correctly interpreted the Natural Gas Act as excluding from federal regulation the whole of the business of production and gathering, including sales for resale in interstate commerce made as a part of that business. This interpretation was required by the words of the Act and by its legislative history. The Commission upon a careful appraisal of all relevant aspects of Phillips' activities found that they were confined to the business of production and gathering and that its sales were made as a part of that business. This finding was fully supported by the evidence. The Court of Appeals erred in rejecting the interpretation

of the statute adopted by the Federal Power Commission and in rejecting the findings of the Commission.

III

On the basis of a record including extensive testimony by the regulatory officials of the producing states, the Commission found that federal regulation of sales such as those made by Phillips would be inconsistent with and conflict with state regulatory functions. This finding was fully supported by the evidence. It represents the considered and expert judgment of the regulatory agency which would enforce federal regulation. The finding establishes that federal regulation of field sales by independent producers and gatherers would inevitably conflict with state conservation measures and thereby nullify the intent of Congress. It therefore supplements and confirms the Commission's conclusion that the Natural Gas Act does not provide for federal regulation of such sales.

IV

The extension of federal regulatory authority to the activities of independent producers and gatherers cannot be justified on the ground that it is necessary to protect consumers against excessive prices. There was no need for such regulation in 1938 when the Natural Gas Act was passed and there is no need for it today.

When Congress enacted the Natural Gas Act, it confined the regulation to the activities of interstate transmission companies and explicitly excluded the business of production and gathering from the scope of the statute. The argument that it is now necessary in the interests of consumers to extend the statute to the business of production and gathering raises grave and complex questions of legislative policy that were not considered or passed upon by Congress.

ARGUMENT

I

THE NATURAL GAS ACT EXCLUDES FROM FEDERAL REGULATION THE WHOLE OF THE BUSINESS OF PRODUCTION AND GATHERING, INCLUDING SALES FOR RESALE IN INTERSTATE COMMERCE MADE AS A PART OF THAT BUSINESS

This is the first time that this Court has been called upon to consider the application of the Natural Gas Act to field sales of natural gas made by a producer and gatherer who does not own or operate an interstate transmission line and whose only activities in the gas industry are the producing, gathering, processing and sale of gas in the producing fields. The ultimate question presented in this case is whether such a producer and gatherer becomes a "natural-gas company", within the meaning of the Natural Gas Act, and subject to federal regulation if, as a part of his business, he sells gas in the producing field to an interstate transmission line for resale.

We submit that the Natural Gas Act does not authorize federal regulation of the business or sales of such an independent producer or gatherer of natural gas. On the contrary it was the intent of Congress to exclude from federal regulation the whole of the business of independent producers and gatherers, including sales for resale in interstate commerce made as a part of that business. That intention is disclosed on the face of the statute by the words Congress used to define the statute's scope, and is confirmed by the legislative history of the statute, by its consistent administrative interpretation, and by the decisions of this Court interpreting and applying its provisions.

A. THE NATURAL GAS ACT ON ITS FACE REGULATES ONLY COMPANIES PERFORMING THE INTERSTATE SERVICE OF TRANSPORTING GAS FROM THE PRODUCING FIELDS TO CONSUMER MARKETS AND EXCLUDES FROM FEDERAL REGULATION THE WHOLE OF THE BUSINESS OF PRODUCING AND GATHERING

The words of the Natural Gas Act must be read in the light of the fact that there are three different operations or economic functions involved in the supplying of gas to ultimate consumers. They are (1) the production and gathering of gas, (2) the interstate transmission of gas by pipe line to consuming markets, and (3) the local distribution of gas for household, commercial and industrial uses.[12] Each of these functions is a different business with special economic, physical and competitive characteristics and problems. Although there are a number of integrated transmission companies that engage in production and gathering as well as transmission, the different phases of the industry are in large part carried on by separate groups of business entities with different characteristics

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[12] See Final Report of the Federal Trade Commission to the Senate of the United States pursuant to S. Res. No. 83, 70th Cong., 1st Sess., Part 84-A (S. Doc. 92, 70th Cong., 1st Sess.), pp. 111, 601, 602 (1935). And see Federal Price Control of Natural Gas Sold to Interstate Pipelines, 59 Yale L. J. 1468, 1469-1470 (1950):

"There are three steps in supplying natural gas to its 14 million users. In the first step, production and gathering, gas is drawn from the earth, often along with oil. It is gathered in by a network of field pipes and processed to remove both nuisances and valuable by-products. • • • All told, about a third of the total marketed production is consumed right in the field. The other two-thirds of the marketed gas moves into pipelines for the second big operation of the industry, long-distance transmission to consumers. About half this volume is consumed within the producing states themselves. Part of the total amount of pipeline gas—whether consumed inside or outside the producing states—is sold directly to individual industrial plants. The rest is passed on to distributing companies for the third operation of the gas business, resale through local mains to household, commercial and industrial users."

that reflect the conditions in the particular phase of the industry in which they are engaged.[13]

When Congress passed the Natural Gas Act it was aware of this tripartite division of the industry.[13a] Congress intended to regulate the middle segment of the industry, that is to say, the business of transmitting gas by pipe line from the producing fields to the consuming markets, including sales for resale made as a part of that business. It intended to exclude from federal regulation the initial function of producing and gathering gas for delivery to the interstate pipe lines—a business thought to be predominantly a matter of local concern to the producing states. It also intended to exclude the final function, the business of distribution to consumers—a business thought to be predominantly a matter of local concern to the consuming states.

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[13] In 1947, according to statistics compiled by the Federal Power Commission, there were 115 interstate transmission companies subject to regulation under the statute. Statistics of Natural Gas Companies, Federal Power Commission, 1947 (United States Government Printing Office), p. v. In the same year there were 2300 independent producers or gatherers who sold natural gas directly to interstate transmission companies (R. 728-731). It has been estimated that there are several thousand additional independent producers or gatherers who do not sell directly to interstate transmission companies. Natural Gas Investigation, Federal Power Commission, Docket No. G-580, Report of Commissioners Smith and Wimberly (United States Government Printing Office 1948), p. 194. Much of the gas sold by these other independent producers is ultimately delivered to interstate transmission companies for interstate transportation to consumer markets.

[13a] "So, broadly speaking, we have in natural gas a situation which no matter how fully and properly integrated will present at both ends problems which are either entirely of local concern, or which are of both local and general public concern, and in between a field of interstate transportation where only through the exercise of Federal jurisdiction can proper solution be obtained." Final Report of the Federal Trade Commission to the Senate pursuant to S. Res. No. 83, 70th Cong., 1st Sess., Part 84-A (S. Doc. No. 92, 70th Cong., 1st Sess.), p. 602 (1935); see also pp. 111, 601.

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The Natural Gas Act begins (Section 1(a)) with a declaration of policy:

> "As disclosed in reports of the Federal Trade Commission made pursuant to Senate Resolution 83 (Seventieth Congress, first session) and other reports made pursuant to the authority of Congress, it is hereby declared that the business of transporting and selling natural gas for ultimate distribution to the public is affected with a public interest, and that Federal regulation in matters relating to the transportation of natural gas and the sale thereof in interstate and foreign commerce is necessary in the public interest."

In this declaration of policy the words "the business of transporting and selling natural gas for ultimate distribution to the public is affected with a public interest" designate the business that Congress intended to regulate. These words describe the business of the interstate transmission lines. They do not describe the business of producing or gathering gas for sale to transmission lines just as they do not describe the business of distributing gas in local markets to ultimate consumers.

Following this declaration of policy, Section 1(b) specifies that the Act shall apply

> "to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural-gas companies engaged in such transportation or sale,"

and then explicitly states that the Act shall not apply

> "to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural gas."

This concluding clause of Section 1(b) excludes from federal regulation both the business of local distribution

and the business of producing and gathering. The clause thus confirms the intent of Congress to regulate only the business of interstate transmission companies. It is that business, as we have seen, that is described by the words used in the declaration of policy. The words "production or gathering" in Section 1(b) describe an entirely different business and should be read as comprehending the whole of the business they describe, including sales in interstate commerce for resale made as a part of that business, and as precluding federal regulation of that business or of such sales. This is the meaning that the Federal Power Commission has always given to the words and which it reaffirmed in this case after a careful review of the legislative history and the relevant decisions of this Court (R. 1741). This reading of the words is consistent both with their plain and ordinary meaning and with the significance that they usually bear in the oil and gas industry.[14]

The subsequent sections of the statute defining the regulatory powers conferred upon the Federal Power Commission provide additional support for this interpretation of the words. The description of these powers shows that they are designed to apply to the business of the interstate transmission companies and not to the business of producing and gathering.

For example, the rate regulation prescribed in Sections 4, 5 and 6 of the Act provides for the traditional form of

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[14] In this case there was substantial evidence before the Commission that in the ordinary usage of the oil and gas industry the words "production or gathering" are used to describe all of the various activities performed by an independent producer and gatherer. See pp. 68-69, *infra*.

"The recognized practices of an industry give life to the dead words of a statute dealing with it." United States v. Maher, 307 U.S. 148, 155. See also Order of Railway Conductors v. Swan, 329 U.S. 520, 525; O'Hara v. Luckenbach S.S. Co., 269 U.S. 364, 370.

public utility regulation—a kind of regulation that historically has been applied to common carriers and to electric, gas and similar public utilities. These sections cover in the classic language of utility legislation the matter of rates and charges.[15] The words used in these sections set standards for rate-making which are appropriate to the transportation services performed by the interstate transmission companies but which would be inappropriate and unsuitable to the economic problems and special characteristics of the business of producing and gathering natural gas. They are words which would normally and naturally be applied to regulation of the cost of transportation or other services; they are inconsistent with the idea of regulating an extractive or mining industry such as the business of producing and gathering natural gas.[16]

The conclusion drawn from the rate-making powers conferred upon the Commission is strengthened by an examination of the provisions of the Act authorizing the Commission to deal with facilities and service. Those provisions, found in Section 7 of the statute, are expressed in words that are applicable to the business of the interstate transmission companies but not applicable to the

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[15] Section 4(a) requires that all rates be "just"; Section 4(b) prohibits undue preferences or unreasonable differences; Section 5 authorizes the Commission to fix rates; and Section 6 authorizes the valuation of property for rate-making purposes. Other provisions incorporate regulatory powers usual in the case of utilities, as for example the power to control depreciation rates, to prescribe systems of accounts, reports, etc.

[16] It is significant that in those instances in which the statute touches any aspect of the gas industry that relates to production and gathering it confers no regulatory authority on the Commission but limits its power to the obtaining of information. Thus Section 11, the only provision of the statute that deals with conservation, explicitly limits the Commission's authority to reporting on action taken by the states in the form of interstate compacts.

business of producing and gathering.[17] These provisions cannot be construed as giving the Commission any authority whatsoever over the facilities used or the service performed in the course of production and gathering. This Court rejected such a suggestion in *Federal Power Commission* v. *Panhandle Eastern Pipe Line Co.*, 337 U.S. 498. This limitation on the Commission's authority is of substantial significance in the present discussion. The sale of gas by an independent producer or gatherer involves more than a price or rate. It also involves such matters as the availability of facilities and continuity of service. If Congress had intended to regulate the business of independent producers or gatherers it would hardly have authorized regulation of one aspect of that business, *i.e.*, the prices charged in sales, and at the same time denied authority to regulate an equally important aspect of sales, *i.e.*, facilities and service. The fact that the latter power is not conferred is persuasive evidence that the statute was not intended to authorize regulation of any aspect of the business of independent producers or gatherers.

So far in this discussion we have seen that the words "production or gathering" in Section 1(b), read in context

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[17] Thus Section 7(a) gives the Commission authority to direct a natural-gas company to extend or improve "its transportation facilities" and to direct the establishment of a "physical connection" of the "transportation facilities" of a natural-gas company with the facilities of "any person or municipality engaged or legally authorized to engage in the local distribution of natural and artificial gas to the public." Section 7(b) requires Commission consent for the abandonment of "facilities subject to the jurisdiction of the Commission, or any service rendered by means of such facilities". Section 7(c), as originally enacted provided that no natural-gas company could, without obtaining a certificate of convenience and necessity, undertake "the construction or extension of any facilities for the transportation of natural gas to a market in which natural gas is already being served by another natural-gas company". In 1942 subsection (c) was amended so as to provide generally that no natural-gas company shall engage in the transportation or sale of gas subject to the jurisdiction of the Commission or undertake the construction or extension of any facilities therefor without a certificate of convenience and necessity.

and against the other provisions of the statute, mean the business of production and gathering. Furthermore, the words comprehend the whole of that business. On the face of the statute there is no restriction, express or implied, that justifies treating the words as meaning anything less. There is nothing, for example, to support a suggestion that the words cover only the physical facilities or operations involved in the business. The words themselves do not suggest that they are so confined and their context provides additional reasons for rejecting such a limitation. Section 1(a) of the Act describes what is to be regulated in terms of a "business". It is reasonable to believe that the provisions of Section 1(b) designating the subject matter that is not to be regulated also describe a business and comprehend all aspects of the business (including sales) and not merely its physical aspects.[18]

There is likewise no merit in the suggestion that the words "production or gathering" cannot cover sales for resale in interstate commerce because Section 1(b) affirmatively subjects such sales to regulation. That part of Section 1(b) providing that the Act shall apply to sales for resale in interstate commerce cannot be read as restricting or limiting the meaning of the words "production or gathering". This becomes apparent when we consider the parallel provision in Section 1(b) relating to transportation. That provision states that the Act shall apply "to the transportation of natural gas in interstate commerce". This language cannot mean that all movement of gas in interstate commerce is subject to regulation.[19] To interpret

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[18] The sales made by an independent producer and gatherer are as much a part of his business as the physical movement of gas. *Cf.* Brown v. Maryland, 12 Wheat. 419, 446-447 (sale an "essential ingredient of importation"); American Sugar Refining Co. v. Louisiana, 179 U. S. 89, 92 (sale an "incident" of manufacture or production).

[19] *Cf.* this Court's treatment of the word "transportation" in the Act to Regulate Commerce of June 29, 1906, as applied to oil pipe lines. The Pipe Line Cases, 234 U. S. 548, 562.

the language in that way would render futile the reference to "gathering" in the concluding clause of the section. The Act by its terms does not purport to apply to intrastate movements of gas; hence, if the word "gathering" is to have any meaning at all it must cover some movements of gas in interstate commerce. The reference to transportation in interstate commerce in the first clause of Section 1(b) must, therefore, be regarded as covering the transportation activities of interstate transmission companies. By the same token the reference to sales for resale in interstate commerce in the first clause of Section 1(b) refers to sales made as a part of the interstate transmission business.

Viewed in this light, and in relation to Section 1(a), the purpose of the affirmative provisions of Section 1(b) becomes clear. Section 1(a) describes the business that is to be regulated, *i.e.*, the interstate transmission business. The function of the affirmative provisions of Section 1(b) is to describe the phases and aspects of that business that are covered by the provisions of the Act; they are not designed to limit or qualify the concluding clause of Section 1(b) which excludes the business of production or gathering from regulation.

It should be noted that in *Interstate Natural Gas Co.* v. *Federal Power Commission*, 331 U.S. 683, this Court stated that even in the case of an interstate transmission company the words "production or gathering" may in appropriate circumstances deprive the Federal Power Commission of jurisdiction to regulate sales for resale in interstate commerce. This indicates that this Court finds nothing on the face of the statute to support either the suggestion that the words are limited to physical facilities and activities or the suggestion that the words can never comprehend sales for resale in interstate commerce.

Just as there is nothing on the face of the statute that justifies an assertion that the words "production or gathering" can never comprehend sales, there is nothing that permits segmenting or dividing the business of pro-

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duction and gathering on some other basis. Nothing in the statute distinguishes between some sales for resale in interstate commerce made as a part of the business and other such sales likewise made as a part of the business. There is no language, for example, that supports a distinction between sales made at the end of production, on the one hand, and sales made at the end of gathering, on the other. The use of the disjunctive in the words "production or gathering" in fact negatives any such distinction. And there is nothing that justifies a distinction between sales made immediately at the end of production and gathering and sales that are made at some other point in the conduct of the business. If such distinctions are asserted the attempt to defend them must appeal entirely to considerations outside the words of the statute because nothing in those words gives such distinctions color or substance. On the face of the statute the only reasonable interpretation to give the phrase "production or gathering" is that it means the whole of the business that it describes, including sales for resale in interstate commerce made as a part of that business.

B. THE LEGISLATIVE HISTORY OF THE NATURAL GAS ACT SHOWS THAT CONGRESS INTENDED TO REGULATE THE INTERSTATE TRANSMISSION COMPANIES AND THAT IT DID NOT INTEND TO REGULATE INDEPENDENT PRODUCERS OR GATHERERS

1. The Federal Trade Commission Report

We know from the words of Section 1(a) of the Natural Gas Act that Congress in passing the statute was responding to the disclosures contained in "reports of the Federal Trade Commission made pursuant to Senate Resolution 83 (Seventieth Congress, first session)". Any discussion of the legislative history of the Act should therefore begin with a consideration of those reports.

The reports were made under a resolution passed by the Senate in February 1928, authorizing the Federal Trade Commission to investigate the operations of public utility corporations and public utility holding companies doing

interstate or international business in power, light or gas.[20] Pursuant to the resolution the Commission conducted a seven-year investigation culminating in a series of reports submitted to Congress in 1934 and 1935. The Final Report of the Federal Trade Commission, dealing with the operations of such corporations in the natural gas industry, was sent to the Senate on December 31, 1935. That document, which was more than 600 pages in length, contained a comprehensive examination of the characteristics, structure, and problems of the natural gas industry.[21]

This report read in its entirety shows that the problems it laid before Congress were problems that existed because of the position and practices of the interstate transmission companies. They were depicted as controlling the "vital link of transportation" that intervened between the producing fields and the consuming markets (FTC Report 610). The report explained that the natural gas industry was "highly competitive at both ends and in two of its three groups of functions", that is, that there was competition in the production and supply of natural gas and in its sale or disposal to consumers, but that the function of transmission or transportation of the natural gas to markets was "one of the least competitive situations to be found involving commodities or public utility service" (*id.* 112). It described the interstate transmission companies as enjoying an "interstate monopoly of transmission" (*id.* 113). The report emphasized that the inter-

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[20] S. Res. No. 83, 70th Cong., 1st Sess., approved February 15, 1928, as extended by S. J. Res. No. 115, 73d Cong., 2d Sess., approved June 26, 1934. These resolutions are set forth in Final Report of the Federal Trade Commission to the Senate pursuant to S. Res. No. 83, 70th Cong., 1st Sess., Part 84-A (S. Doc. No. 92, 70th Cong., 1st Sess.) pp. v-vi.

[21] Final Report of the Federal Trade Commission to the Senate pursuant to S. Res. No. 83, 70th Cong., 1st Sess., Part 84-A (S. Doc. No. 92, 70th Cong., 1st Sess.).

state transmission lines were controlled or dominated by a small group of holding companies which likewise had interests in the producing and distribution aspects of the industry.

The report also explained that the states were unable to regulate the prices charged by the interstate transmission companies at the city gates because of Supreme Court decisions holding that under the Commerce Clause such transactions were not subject to state regulation. Consequently, the report stated, "the interstate pipe line companies * * * are at present virtually free from regulation * * *" (*id.* 613-614). It concluded that "the need for federal regulation of the activities and operations of such interstate pipe line companies appears too evident to require further discussion" (*id.* 614).

In contrast the report did not assert that any problems requiring the exercise of federal power existed by reason of the position or practices of independent producers and gatherers of natural gas. The report discussed conditions in the producing fields and the activities of independent producers and gatherers, but it did not suggest that the prices charged by such producers and gatherers were excessive or non-competitive or should be regulated by federal authority. Indeed the report pictures the independent producers or gatherers as standing in need of protection against the monopolistic, predatory and discriminatory practices of the interstate transmission companies (*id.* 185-195, 583, 590-592, 602, 608, 611). The report suggested that the remedy for these problems lay primarily in state laws and interstate compacts providing for unitized operation, equitable and ratable taking, and similar measures (*id.* 616).

It thus appears that the Federal Trade Commission Report presented to Congress for its consideration the problems created by the activities of the interstate transmission companies which were engaged in transporting

gas from the producing fields to consumer markets. It was that phase or segment of the industry, not the business of independent producers or gatherers, that was described as requiring federal regulation. As the subsequent legislative record shows, it was to that phase or segment of the industry that Congress directed its attention.

2. The Committee Hearings and Reports

On March 6, 1936, Congressman Lea introduced H. R. 11662, a bill to regulate the natural gas industry. The provisions of this bill were subsequently changed in certain respects, but the bill has been described by this Court as "substantially similar to the Natural Gas Act." *Federal Power Commission* v. *Panhandle Eastern Pipe Line Co.*, 337 U.S. 498, 505, and this Court has treated the hearings on the bill as an integral part of the legislative history of the statute.[22] *Federal Power Commission* v. *Panhandle Eastern Pipe Line Co.*, *supra;* see also *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591, 610, n. 19; *Federal Power Commission* v. *East Ohio Gas Co.*, 338 U.S. 464, 472, n. 12.

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[22] The different steps in the progress of the legislation were:

1. H. R. 11662 was introduced in the House of Representatives in the 74th Congress, 2d Session.

2. After hearings H. R. 11662 was revised in certain respects, and introduced in the same session as H. R. 12680. For a discussion of certain of the revisions see note 27, p. 34 *infra*. H. R. 12680 was reported by the House Committee on Interstate and Foreign Commerce, but not acted upon by Congress.

3. H. R. 4008, which was the same as H. R. 12680, was introduced in the 75th Congress, 1st Session. Hearings were held on the bill by the Committee.

4. H. R. 4008 was revised in minor respects, introduced as H. R. 6586, and reported by the Committee, without further hearings.

5. H. R. 6586 was passed by the House with amendments on July 1, 1937, and by the Senate, with certain amendments, on June 7, 1938. The amendments were settled in conference and the bill as finally agreed to was approved by the President on June 21, 1938.

In the hearings before the House Committee on H. R. 11662 the first witness was Dozier A. DeVane, then Solicitor of the Federal Power Commission, who appeared at the request of the Chairman of the Committee, and testified on the scope of the bill's provisions. His testimony is of particular significance because representatives of the Federal Power Commission had participated in the drafting of the proposed legislation.[23]

In explaining the bill Mr. DeVane expressly stated that under Section 1(b) the Commission would have no jurisdiction over the rates for natural gas "that are paid in the gathering field." *Hearings before Subcommittee of Committee on Interstate and Foreign Commerce on H. R. 11662,* 74th Cong., 2d Sess., p. 28 (1937).

He made the same point again in the following colloquy with a member of the Committee (*id.* 34):

> "Mr. Cole. Does this bill give anywhere the Commission power over the source of natural gas in the different fields in a manner which we might call comparable to that which your Commission now has over hydro-electric generating plants?
>
> "Mr. DeVane. It does not; no. It does not attempt to regulate the gathering rates or the gathering business. Section 11, I believe it is, of the bill deals with that."[24]

At a later point in the hearings the Chairman of the Committee again raised the point and Mr. DeVane again

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[23] See DeVane, Highlights of Legislative History of the Federal Power Act of 1935 and the Natural Gas Act of 1938, 14 Geo. Wash. L. Rev. 30, 38-39 (1945).

[24] Mr. DeVane then observed that Section 11 limits the Commission to action through the producing states:

"But Section 11 deals with State compacts, not in the sense of prescribing what State compacts should be but simply gives to the Commission authority to investigate and report to the Congress upon the State compacts that are submitted for approval. But the bill itself does not attempt to regulate either the gathering end or the distributing end of the business; * * *." (*ibid.*)

explicitly stated that the legislation did not authorize regulation of field prices (*id.* 42-43):

> "Mr. Lea. Mr. DeVane, I would like to go back just a moment. Of course, it is a question of regulation. Suppose that the A company owns a gas supply and the B company transmits it into another State, distributes it to a local company for distribution. Now suppose the question arises as to whether or not the charges which the A company makes against the B company for the gas is reasonable. What, if any, authority would the Commission have on that question, under this bill? Do you get my question?
>
> "Mr. DeVane. Yes; if I understand your question, concerning the price paid to the A company, there is no control of the gathering rate; the Commission would not have jurisdiction. That price is fixed by competitive conditions that exist in the field. But it matters not how many different ownerships there may be between the time the gas starts to move in interstate commerce and gets to the city gates. Ownership might change a dozen times—A company sell to B, and B company sell to C—all those rates would be subject to regulation.[25]

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[25] In this passage Mr. DeVane, after again stressing that the Commission would not have jurisdiction over the price paid to the producer and gatherer, recognized that where more than one pipe line company participated in the interstate transmission to the consumer market, all such pipe lines were subject to federal regulation. As the hearings indicate, in the case of some consumer states, such as Illinois, one interstate pipe line which carried gas from the producing field sold the gas at some point in the interstate journey to another interstate pipe line which in turn carried it the remainder of the distance and sold to the distributing company. See Hearings before the Committee on Interstate and Foreign Commerce on H. R. 4008, 75th Cong., 1st Sess., pp. 34, 56-57 (1937). Mr. DeVane's quoted statement shows that the legislation was designed to cover this situation. To remove any possibility that any of the sales by interstate pipe lines would not be subject to Federal jurisdiction, the bill was amended, with Mr. DeVane's approval, to emphasize that it covered all sales by the interstate pipe lines and not just the final sale for resale to the public (*id.* 57).

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"Mr. Lea. Well, when the supply company is brought before the Commission in an action to regulate its rates, and they say, 'We have got to pay so much for gas; we cannot control that price which they charge us, and we have to charge a higher price delivered to the buyer.'

"Does the Commission have any power over that?

"Mr. DeVane. No; not the price that is paid to the gatherer, to the man that produces it; that is binding if the transaction is at arm's length. If the transaction is not at arm's length, of course, its reasonableness may be inquired into, under the decisions of the Supreme Court."

No other witness and no member of the Committee, either in the hearings on H. R. 11662 or in the subsequent hearings on H. R. 4008, disagreed with or disputed Mr. DeVane's statement that the proposed legislation did not extend federal control to the field prices of natural gas. On the contrary there was testimony from other witnesses in both hearings recognizing that the legislation was directed to the practices of the interstate transmission companies and that the prices to be regulated were the prices charged by those companies with particular reference to their prices at city gates.[26] No independent

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[26] Thus in the hearings on H. R. 11662, J. D. Battle, testifying on behalf of the National Coal Association, said (*id.* 72):

"Consequently, the only phase of the industry, as I see it, that it is proposed to regulate is after the gathering ceases and the gas is turned into a main line, so to speak, until it reaches the city gate, and only then when it is moving in high-pressure mains across State lines."

And in the hearings on H. R. 4008, H. R. Booth, testifying for the Illinois Commerce Commission, said:

"The wholesale rate which is covered by the act would cover, as I understand it, any wholesale rate or charge under which a transmission company or a producing and transmission company sells natural gas and which either transmits it in interstate commerce to either a distributing company or another

producer or gatherer testified or submitted a statement in any of the hearings and there was no suggestion at any point in the hearings that the field prices of such producers and gatherers were to be subject to federal regulation.

In view of Mr. DeVane's position, the direct and explicit tenor of his statements as to the bill's scope, and the acceptance of those statements by the members of the House Committee, his testimony provides strong evidence that the members of the congressional committee that considered and reported the bill believed that it did not regulate the prices charged in the field by independent producers and gatherers.[27]

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wholesale company." (Hearings before the House Committee on Interstate and Foreign Commerce on H. R. 4008, 75th Cong., 1st Sess. p. 39 (1937)).

For testimony indicating that the evils thought to require the exertion of regulatory power were those arising from the practices of the interstate transmission companies, see particularly the testimony of William T. Chantland of the Federal Trade Commission in the hearings on H. R. 11662 (pp. 51-52, 56-57).

[27] No hearings were held on the legislation by the Senate Committee.

In the court below it was contended that Mr. DeVane's testimony should be disregarded because H. R. 11662, to which the testimony was directed, defined the scope of the Act in terms different from those used in the Natural Gas Act. The short answer to that argument is that this Court has described the bill as "substantially similar" to the Act, and has relied upon Mr. DeVane's testimony in discussing the legislative history. Federal Power Commission v. Panhandle Eastern Pipe Line Co., 337 U.S. 498, 505, n. 7.

The changes made in H. R. 11662 do not impair the value of Mr. DeVane's testimony. The argument to the contrary rests on two assumptions: (1) that H. R. 11662 did not authorize the regulation of sales in interstate commerce, and (2) that the scope of the Act as defined in Section 1(b) of H. R. 11662 was extended by the changes made in the form of that section. Both assumptions are erroneous. Section 4(a)(b) of H. R. 11662 authorized the regulation of sales in interstate commerce. The words of Section 1(b) were changed not to extend the Act's coverage but to make certain that the provisions of the Act applied only to interstate transmission companies. Section 1(b) of H. R. 11662 provided that the

H. R. 6586, the bill which became the Natural Gas Act, was reported by the House Committee on Interstate and Foreign Commerce, on April 28, 1937 (H. Rep. No. 709,

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Act should apply to the transportation of natural gas in "high pressure mains" in interstate commerce and to natural-gas companies engaged in such transportation, but should not apply to the distribution of natural gas moving locally in low pressure mains or to the facilities used for such transportation or to the production of natural gas. In thus describing the scope of the statute in terms of transportation in "high pressure mains" the draftsmen of H. R. 11662 intended to describe the activities of the interstate transmission companies, since those terms were regarded as an apt description of the transportation service provided by such companies. Compare Federal Power Commission v. East Ohio Gas Company, 338 U.S. 464, 470, n. 10.

The language of Section 1(b) was criticised in the hearings on H. R. 11662 on the ground that gas was sometimes delivered by local distributing companies to consumers from high pressure mains and that the bill's language would authorize federal regulation of such transactions, and that therefore "• • • the purpose of Congress to reserve the local field to the local authorities would not be accomplished • • •." Hearings on H. R. 11662, pp. 91, 92. Therefore when H. R. 11662 was revised and reintroduced as H. R. 12680, the language of Section 1(b) was changed and the scope of the Act stated in terms substantially similar to those now found in Section 1(b) of the statute. The change was made so that federal regulation would not extend to any aspect of local distribution. At the same time the word "gathering" was added to the exclusionary phrase in Section 1(b)—a change that provided additional support for Mr. DeVane's description of the scope of the bill.

These changes in Section 1(b) were embodied in H. R. 4008 when it was introduced in the 75th Congress. The changes were not regarded as changes in substance but as revisions in form designed to carry out the draftsmen's original intent. This is shown by the fact that at the beginning of the hearings on H. R. 4008 the Chairman of the House Committee stated that there was only one substantial difference between that and H. R. 11662, *i.e.*, that H. R. 4008 provided for certificates of convenience and necessity. Hearings before the Committee on Interstate and Foreign Commerce on H. R. 4008, 75th Cong., 1st Sess., pp. 1, 23 (1937).

It is not to be supposed that this statement would have been made if the changes in the bill were understood as subjecting to regulation a whole segment of the industry clearly not covered by the original bill.

75th Cong., 1st Sess.). The report begins by explaining that (*id.* 1):

> "• • • the present bill would for the first time provide for the regulation of natural-gas companies transporting and selling natural gas in interstate commerce."

Having thus indicated that the bill was intended to regulate the interstate transmission companies, the report proceeded to point out that it was designed to reach the interstate transactions of those companies, particularly sales at the city gate, which were immune from state regulation. On this point the report said that the bill (*id.* 1-2):

> "• • • confers jurisdiction upon the Federal Power Commission over the transportation of natural gas in interstate commerce, and the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use. The States have, of course, for many years regulated sales of natural gas to consumers in intrastate transactions. The States have also been able to regulate sales to consumers even though such sales are in interstate commerce, such sales being considered local in character and in the absence of congressional prohibition subject to State regulation. (See *Pennsylvania Gas Co.* v. *Public Service Commission* (1920), 252 U.S. 23.) There is no intention in enacting the present legislation to disturb the States in their exercise of such jurisdiction. However, in the case of sales for resale, or so-called wholesale sales, in interstate commerce (for example, sales by producing companies to distributing companies) the legal situation is different. Such transactions have been considered to be not local in character and, even in the absence of Congressional action, not subject to State regulation. (See *Missouri* v. *Kansas Gas Co.* (1924), 265 U.S. 298, and *Public Service Commission* v. *Attleboro Steam & Electric Co.* (1927) 273 U.S. 83.) The basic purpose of the present legislation is to occupy this field in which the Supreme Court has held that the States may not act."

The report then pointed out (*id.* 2):

> "The bill takes no authority from State commissions, and is so drawn as to complement and in no manner usurp State regulatory authority, and contains provisions for cooperative action with State regulatory bodies."

It is also significant that the report stated (*id.* 3):

> "The bill provides for regulation along recognized and more or less standardized lines. There is nothing novel in its provisions, and it is believed that no constitutional question is presented."[28]

In commenting on the provisions of Section 1(b) which excluded from regulation both the business of local distribution and the business of production or gathering, the House Report said (*ibid.*):

> "The quoted words are not actually necessary, as the matters specified therein could not be said fairly to be covered by the language affirmatively stating the jurisdiction of the Commission * * *."

This statement is again a recognition that the legislation was not directed at the operations at each end of the natural gas industry, *i.e.*, producing or gathering at the one end, and local distribution at the other, but was designed to regulate only the middle segment of the industry, the transmission and sale of gas by the interstate pipe lines.

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[28] The Committee would hardly have said that the legislation contained "nothing novel" and provided for regulation along "recognized and more or less standardized lines" if it had believed that it was for the first time extending public utility regulation to the business of producing and gathering natural gas. That is essentially a mining or extractive business. It differs radically from the business of the interstate transmission companies which consists chiefly of providing a transportation service and which closely resembles the industries historically regulated as public utilities.

One passage in the Committee Report has been seized upon by proponents of federal regulation to support the contention that the statute was designed to regulate the field prices of independent producers or gatherers. This is the passage, quoted at p. 36, *supra*, which cites *Missouri* v. *Kansas Natural Gas Co.*, 265 U.S. 298, and *Public Utilities Commission* v. *Attleboro Steam & Electric Co.*, 273 U.S. 83, and states that the basic purpose of the legislation is "to occupy this field in which the Supreme Court has held that the States may not act". The argument runs that this passage shows that Congress intended to close a "gap" in regulatory authority; that the states do not have, or at least when the Act was passed did not have, authority to regulate the prices charged in the field by independent producers or gatherers; and hence that it necessarily follows that Congress intended the Natural Gas Act to regulate those prices.[29]

This argument assumes that the words "this field" in the Committee Report comprehend the business of independent producers or gatherers. This assumption is not supported by the words of the Committee Report and it is contradicted by the whole course of the legislative history.[30] The question of what segment of the gas industry

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[29] This argument was heavily relied upon in the opinion of the court below (R. 1843-1847). See pp. 61-63 *infra*.

[30] The parenthetical reference in the Committee Report to "sales by producing companies to distributing companies" does not refer to sales by independent producers or gatherers. Read in context that statement refers to sales to local distributing companies after interstate transportation by interstate transmission companies which produce their own gas. In the instances during the hearings where there was mention of sales by "producing companies" the setting discloses that, as in the Committee Report, the reference was to an integrated transmission company which also produces gas. See, *e.g.*, the statement that the "wholesale rate" subject to regulation under the bill was the rate "under which either a transmission company or a producing and transmission company sells natural gas". Hearings before the Committee on Interstate and Foreign Commerce on H. R. 4008, 75th Cong., 1st Sess., p. 39 (1937).

was to be regulated was essentially an economic question and Congress decided it on economic grounds. As we have seen the Federal Trade Commission Report had disclosed that the evils existing in the gas industry were a result of the position and practices of the interstate transmission companies. It was the business of those companies that Congress decided to regulate; it considered questions of constitutional power only as they bore on the question of which activities of the transmission companies had to be regulated by Congress and which could be left to the regulatory power of the states.

No evidence was presented to Congress of practices by independent producers or gatherers that had created or threatened to create economic problems or evils that required federal regulation. Because there were no evils in that aspect or function of the industry that required correction there was no occasion for Congress to consider whether there was any so-called "gap" in the power to regulate independent producers or gatherers. The "gap" in regulatory authority was conceived by Congress in terms of the activities of the interstate transmission companies and not in terms of the activities of independent producers or gatherers. This is indicated by the decisions that were cited in the Committee Report as evidencing the lack of state authority, *i.e., Missouri* v. *Kansas Natural Gas Co.*, 265 U.S. 298, and *Public Utilities Commission* v. *Attleboro Steam & Electric Co.*, 273 U.S. 83. Those cases dealt with the authority of the states to regulate the activities of companies engaged in the interstate transmission of gas or electric energy to or into consuming states; they did not relate in any way to the authority of states to regulate the activities of independent producers or gatherers of natural gas.[31]

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[31] Missouri v. Kansas Natural Gas Co., 265 U.S. 298, involved a company producing and purchasing gas in Oklahoma and Kansas and transporting gas for sale in Missouri to distributing companies. In Public Utilities Commission v. Attleboro Steam & Electric Co., 273 U.S. 83, it was decided that Rhode Island could not

The attention of Congress was therefore not called to any "gap" in the authority to regulate the activities of independent producers or gatherers. There was no reason for Congress to consider such a gap because it was proceeding upon the assumption that the activities of independent producers or gatherers did not require federal regulation.

The limits which Congress placed on the regulation it imposed on the interstate transmission companies, which were operating within the unregulated field referred to in the Committee Report, also show that Congress could not have been considering any regulation of independent producers or gatherers. As we have seen, the Report stated that the Act was intended "in no manner [to] usurp State regulatory authority." See p. 37, *supra.* Congress knew that the states had, as this Court said in *Federal Power Commission* v. *Panhandle Eastern Pipe Line Co.,* 337 U.S. 498, 510, 513, "delegated broad and elaborate power to their regulatory bodies on all aspects of producing gas."[32] One of the major purposes of the

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regulate a sale of electric energy at the Massachusetts state line for transmission and subsequent distribution in Massachusetts. In Panhandle Eastern Pipe Line Co. v. Public Service Commission of Indiana, 332 U.S. 507, 514, this Court cited the two cases for the proposition that by 1938 the courts had held that the states "could not intrude" on "service interstate to local distributing companies for resale." See also Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591, 610.

[32] When the statute was passed it had long been recognized that the states had a special interest in natural gas and that its regulation touched rights of "an essentially local character." See Ohio Oil Company v. Indiana, (No. 1), 177 U. S. 190, 211-212; Lindsley v. Natural Carbonic Gas Co., 220 U. S. 61; Pierce Oil Corp. v. Phoenix Refining Company, 259 U. S. 125; Walls v. Midland Carbon Co., 254 U. S. 300, 319; Bandini Petroleum Co. v. Superior Court, Los Angeles County, Calif., 284 U. S. 8; Henderson Co. v. Thompson, 300 U. S. 258, 264. It had also long been recognized

inclusion of the "production or gathering" exemption was to make sure that even the regulation of the interstate transmission companies should not interfere with this conservation regulation. It is inconceivable that Congress could have taken this care to prevent the regulation of the interstate transmission companies from interfering with the state programs and at the same time have intended to subject to regulation the business of the independent producers and gatherers; the nature of that business is such that any federal regulation would necessarily conflict and interfere with the producing states' regulatory programs. See pp. 73-84, *infra*.

3. The Debates

H. R. 6586 was passed by both houses of Congress without extensive debate, the bill being described in both houses as non-controversial in nature (81 Cong. Rec. 6726; 83 Cong. Rec. 8347). The debates reflect the same views about the purpose and scope of the legislation that were expressed in the earlier stages of the legislative history. Thus, the bill was regarded as directed at the practices of the interstate transmission lines that were engaged in moving gas by pipe line from the producing fields to the consuming markets. The bill's sponsors made this point specifically in their descriptions of the bill and referred particularly to the necessity for federal regulation of the prices charged by the interstate transmission companies

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that the states might regulate matters of local concern even though the regulation affected interstate commerce. Willson v. Black-bird Creek Marsh Co., 2 Pet. 245; Cooley v. Board of Wardens of the Port of Philadelphia, 12 How. 298; South Carolina State Highway Department v. Barnwell Brothers, Inc., 303 U. S. 177, 184-185, 188-189.

In reliance on these principles this Court held in Cities Service Gas Co. v. Peerless Oil & Gas Co., 340 U. S. 179, that in the interests of conservation the State of Oklahoma could require producers to realize minimum prices for gas sold in interstate commerce. See pp. 63-66, *infra*.

at the city gates.[33] There was no reference in the debates to any problems created by the activities of independent producers or gatherers and no assertions that the bill was intended to regulate their activities or the prices that they charged in the field for gas they produced or gathered.[34]

In the House of Representatives the Chairman of the House Committee on Interstate and Foreign Commerce, took the lead in presenting the bill. He stated that the report of the Federal Trade Commission provided the "statistical background that gives the setting for this legislation"; that "the city-gate rates in an interstate shipment could be controlled by the Federal Power Commission under this bill" and that the "State commission does not have that power now"; that "this bill takes nothing from the State commissions"; and that the bill "does not apply to the production and gathering of gas" (81 Cong. Rec. 6721).[35]

Other members of the committee that had reported the bill repeated and enlarged upon the same themes. It was

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[33] One of the aspects of pipe line service singled out for attack was discrimination by interstate pipe lines in the city gate rates charged different communities. 81 Cong. Rec. 9315 (1937).

[34] Significantly, the House was told that the "only provision in the bill which seems to look to the conservation of the natural gas resources of the country is that contained in the provision relating to the State compacts [Section 11]." 81 Cong. Rec. 6726 (1937).

In Federal Power Commission v. Panhandle Eastern Pipe Line Co., 337 U. S. 498, 512, n. 16, this Court pointed out that in 1937 while Congress was considering the passage of the Natural Gas Act, another bill was introduced in both Houses of Congress which would have extended the authority of the Federal Power Commission "to the procurement of natural gas" for interstate transmission. This Court commented "The provisions of this bill, however, failed of adoption; instead Congress enacted § 1(b) with its specific exemptions from the coverage of the Act."

[35] Others also pointed out that the bill was the culmination of the Federal Trade Commission investigation (*id.* 6724, 6725).

said that the "State commissions have had no power over the interstate activities of the pipe-line companies" (*id.* 6726) and that they were "charging what they please at the city gate" (*id.* 6724). Congressman Halleck of Indiana explained that "in many instances the transportation company, transporting in interstate commerce, has charged a rate which is higher than is deemed fair and reasonable" (*id.* 6723).[36] Another proponent of the bill stated its purpose in the following terms (*id.* 6726):

> "It gives the Federal Power Commission power to fix the cost of the transportation of natural gas shipped in interstate commerce and the wholesale price which may be charged for it at the consuming centers."

In the Senate, where there was less extensive debate than in the House, the scope of the legislation was explained in similar terms. The Chairman of the Committee on Interstate Commerce, in explaining the bill, said (*id.* 9312):

> "Mr. Wheeler. It does not attempt to regulate the producers of natural gas or the distributors of natural

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[36] Congressman Halleck explicitly stated that the bill would authorize regulation of the prices at the city gates in the following passage (*id.* 6723):

> "In the past few years the interstate transportation of gas in large pipe lines at high pressure had been growing by leaps and bounds. Gas is brought from the producing areas in these pipe lines and sold at the city gates to the public utilities which distribute the gas to the consumers. It is obvious the distribution of the gas by the local distributing company is subject to State regulation and the interests of the consumers are protected by State regulation. However, the transportation of gas in interstate commerce in the pipe lines and its sale to the distributing companies for resale is not subject to State regulation, and as a result, we have had a situation under which the price charged the distributing company at the city gate has been fixed wholly by the judgment, discretion, or action of the interstate company. It is charged that in many cases that price is excessive. This bill seeks to regulate those prices."

gas; only those who sell it wholesale in interstate commerce.

* * *

"Mr. Austin. Is the bill limited in its scope to the regulation of transportation?

"Mr. Wheeler. Yes; it is limited to transportation in interstate commerce, and it affects only those who sell gas wholesale."

At a later point in the debate, Senator Wheeler framed the problem to which the bill was directed as follows (*id.* 9314):

"The purpose of the bill is to help the State commissions and the people of the country find out what is the cost of transporting natural gas to the larger cities, such as Detroit, Chicago, Cleveland, and New York City. It does not do any good to give the Illinois commission the power to regulate the price of gas in the city of Chicago if they can be held up—and that is all that it is—by pipe-line companies which ship the gas to Chicago and be told. 'It is going to cost the city of Chicago so much at wholesale for this gas.' What good does it do the people of Chicago if they cannot reach the wholesale price and do something to regulate the pipe-line companies which transport the gas into the city of Chicago?"[37]

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[37] In voicing agreement with Senator Wheeler, other Senators expressed the problem in similar terms. See *e.g.*, 81 Cong. Rec. 9315:

"* * * As the Senator says, when an effort is made to regulate the price of gas, we will say, by way of illustration, in Terre Haute, Ind., just across the Illinois line, as far as the Public Service Commission of the State of Indiana can go is to ascertain what the wholesale price is to the gas company in Terre Haute. That may be 50 or 60 cents a thousand; but when they say, 'Produce your contract and let us look into the cost of getting that gas to the gateway at Terre Haute, Ind.'; the company replies, 'Oh, no; that is interstate commerce, and you cannot enter into that field.'

"Therefore, as the Senator has pointed out, our Public Service Commission cannot determine whether or not the people of Terre Haute are being charged a fair rate for their gas, because it cannot determine the fairness of the wholesale rate that is charged at the gate at Terre Haute."

This review of the legislative history has not been contrived by culling particular passages from the hearings, the Committee Report and the debates without regard to the context of the passages or their relationship to other passages dealing with similar subject matter. Each of the particular statements that has been quoted or paraphrased in the discussion is significant not in isolation but because of the light it throws on the legislative history viewed as an entirety and in all of its aspects. That history beginning with the Federal Trade Commission Report and ending with the debates in both Houses of Congress, read as a whole, provides a solid basis for appraising the intent of Congress. The appraisal confirms and supports the regulatory plan and purpose disclosed on the face of the statute. Congress intended to regulate the business of the interstate transmission companies which were engaged in the transportation of gas in interstate commerce from the producing fields to consuming markets—the business that is described in Section 1(a) of the statute as "the business of transporting and selling natural gas for ultimate distribution to the public." Congress did not intend to regulate the business of independent producers or gatherers, and specifically it did not intend to fix the prices at which they sold their gas in the field.[38]

C. THE FEDERAL POWER COMMISSION'S CONSISTENT ADMINISTRATION OF THE NATURAL GAS ACT CONFIRMS THE ABSENCE OF COMMISSION JURISDICTION OVER THE BUSINESS OF INDEPENDENT PRODUCERS AND GATHERERS, INCLUDING SALES BY THEM FOR RESALE

The first case involving the status of an independent producer or gatherer to come before the Federal Power Commission after the passage of the Natural Gas Act was *In the Matter of Columbian Fuel Corporation,* 2 F.P.C.

[38] This is the view reached by independent commentators who have examined the legislative history. See Berger and Krash, Status of Independent Producers under the Natural Gas Act, 30 Tex. L. Rev. 29 (1951); Comment, 59 Yale L. J. 1468 (1950); Note, 52 Col. L. R. 135 (1952); Note, 22 Geo. Wash. L. Rev. 118 (1953).

200, decided June 29, 1940. In that case Columbian was engaged in producing and gathering natural gas and selling and delivering the gas at the termini of its gathering lines to an interstate transmission company. The question was whether the Commission was authorized by the statute to regulate these sales; in the words of the Commission the issue was "whether the Natural Gas Act confers on the Federal Power Commission jurisdiction over a company engaged solely in the production and gathering of natural gas when such company is also engaged in the sale of such gas in interstate commerce."

Representatives of the producing and consuming states and of associations of independent producers, as well as the companies concerned, participated in the hearing before the Commission. After a review of the terms of the statute and its legislative history the Commission, with one member dissenting, concluded that Congress intended to regulate only "pipe line" companies and that it was (*id.* 208):

> "not the intention of Congress to subject to regulation under the Natural Gas Act all persons whose only sales of natural gas in interstate commerce, as in this case, are made as an incident to and immediately upon completion of such person's production and gathering of said natural gas and who are not otherwise subject to the jurisdiction of this Commission."

It is to be noted that three of the four Commissioners who joined in this decision were members of the Federal Power Commission at the time the Natural Gas Act was passed and that one of the three (Commissioner Seavey) had been designated by the Commission to assist the Congressional committees in drafting the bills that ultimately resulted in the passage of the statute.[39]

A few months later the Commission was called upon to consider the application of the statute to a company

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[39] DeVane, Highlights of Legislative History of the Federal Power Act of 1935 and the Natural Gas Act of 1938, 14 Geo. Wash. L. Rev. pp. 30, 39 (1945).

engaged in production and gathering and also in the interstate transmission business. *In the Matter of Billings Gas Co.*, 2 F.P.C. 288, decided October 15, 1940. The Commission held that a company that produced and gathered natural gas and then transported the gas beyond the termini of its gathering lines through a transmission line to a state border, where it sold the gas to another interstate transmission company, was a natural gas company and subject to federal regulation. The Commission distinguished *Columbian Fuel Corporation*, saying that in that case (*id.* 289):

> "There was no transportation of natural gas in interstate commerce beyond the termini of the gathering lines. A person, however, engaged in the production and gathering of natural gas and the subsequent transportation, or transportation and sale, thereof in interstate commerce, would not fall within the same category."

The two decisions taken together established a jurisdictional test for determining whether on the facts of a particular case sales were subject to regulation under the statute. The test was whether the sales were "made as an incident to and immediately upon completion of" the production or gathering process as the *Columbian* case or were made by a company that is "engaged in the production and gathering of natural gas and the subsequent transportation, or transportation and sale, thereof in interstate commerce" as in the *Billings* case.

In the thirteen years that have followed since the Commission decided the *Columbian* and *Billings* cases it has adhered to this jurisdictional test and has consistently construed the Natural Gas Act as not authorizing the regulation of sales made by independent producers and gatherers as part of their business. *Repollo Oil Co.*, 2 F.P.C. 1004 (1941); *Sinclair Prairie Oil Co.*, 2 F.P.C. 1009 (1941); *The Fin-Ker Oil and Gas Production Co.*, 6 F.P.C. 92 (1947); *Tennessee Gas and Transmission Company and The Chicago Corporation*, 6 F.P.C. 98 (1947); *Kansas-Nebraska Natural Gas Co., Inc.*, 6 F.P.C. 664 (1947);

R. J. and D. E. Whelan, 6 F.P.C. 672 (1947); *Hassie Hunt Trust*, 6 F.P.C. 835 (1947); *Sinclair Prairie Oil Co.*, 6 F.P.C. 1059 (1947); *La Gloria Corp.*, 7 F.P.C. 349 (1948); *The Superior Oil Co.*, 7 F.P.C. 627 (1948). Throughout this period the Commission has not in a single instance regulated or attempted to regulate field sales of gas made by independent producers or gatherers to interstate transmission companies.[40]

The fact that the Federal Power Commission has thus consistently construed the statute as not providing for federal regulation of field sales of independent producers and gatherers is highly persuasive that Congress did not authorize such regulation. See *Federal Power Commission* v. *Panhandle Eastern Pipe Line Co.*, 337 U.S. 498, 513; *Federal Trade Commission* v. *Bunte Brothers, Inc.*, 312 U.S. 349, 351-352; *National Labor Relations Board* v. *Hearst Publications, Inc.*, 322 U.S. 111, 131; *United States* v. *Chicago North Shore & Milwaukee R. Co.*, 288 U.S. 1, 13-14; *Norwegian Nitrogen Products Co.* v. *United States*, 288 U.S. 294, 315; *United States* v. *American Trucking Ass'ns, Inc.*, 310 U.S. 534, 549; *Levinson* v. *Spector Motor Service*, 330 U.S. 649, 667, 672.

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[40] In the court below it was argued that certain statements made by the Commission in Interstate Natural Gas Co. Inc., et al., 3 F.P.C. 416, were inconsistent with the interpretation of the statute it adopted in the Columbian case and the other cases cited above. It is clear, however, that the Commission's opinion in the Interstate case did not abandon or change the jurisdictional rule laid down in the Columbian case. On its facts the Interstate case was like the Billings case; the sales there were made by an interstate transmission company after transportation in interstate commerce in the statutory sense (3 F.P.C. 432-433). In its opinion in the Interstate case the Commission did not refer to the Columbian case or suggest that it was overruling or abandoning the jurisdictional test there laid down. The four Commissioners who joined in the opinion in the Interstate case also joined in the opinion in the Columbian case; they could hardly have intended to overrule the latter decision *sub silentio*, particularly since that decision was later followed in a number of cases.

D. THE DECISIONS OF THIS COURT RECOGNIZE THAT THE NATURAL GAS ACT DOES NOT AUTHORIZE ANY DIRECT FEDERAL REGULATION OF THE BUSINESS OF PRODUCING AND GATHERING

We have shown above that the Natural Gas Act was intended by Congress, and is framed, to provide a standardized form of utility regulation of the interstate service of transmitting natural gas to consumer markets. The major decisions of this Court under the Act have been concerned principally with the difficult problems created by the fact that the operations of many of the interstate pipe line companies subject to this regulation are not confined to the transmission business. These decisions do not decide this case.[41] Nevertheless they do support the interpretation of the Act set forth above.

Taken as a group and read in the light of the problems with which the Court was concerned, these cases demonstrate an awareness of three fundamental aspects of the Act. They are:

(1) That the companies regulated are the transmission companies performing the interstate service of transporting gas to consumer markets.

(2) That the regulation of the interstate transmission companies is not to extend federal authority into any area in which the states are constitutionally competent to act for any purpose.

(3) That the Act precludes any direct regulation of the business of producing and gathering.

In *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591, and *Colorado Interstate Gas Co.* v. *Federal*

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[41] The question raised by this case was specifically reserved by this Court in Interstate Natural Gas Co. v. Federal Power Commission, 331 U. S. 682, 690-691, n. 18. There this Court, referred to the Columbian case, 2 F.P.C. 200, and the Billings case, 2 F.P.C. 288, and said: "We express no opinion as to the validity of the jurisdictional test employed by the Commission in these cases."

Power Commission, 324 U. S. 581, this Court dealt with the problem of rate regulation of interstate transmission companies which also own and operate producing and gathering facilities.[42] This Court held in those cases that the Natural Gas Act does not require the Federal Power Commission to use any particular method of rate fixing, and that accordingly the responsibilities of a reviewing court are limited to determining whether the result or the impact of the regulation is arbitrary or constitutionally unfair. These holdings were based on the failure of Congress to require any particular method of rate regulation on the face of the Act. In both cases this Court pointed out that the Act was framed in the traditional and standardized language used for the regulation of transportation services. 324 U. S. at 601; 320 U. S. at 616.[43]

In the *Colorado Interstate* case the transmission line contended that the production or gathering exemption required the Commission to exclude from the rate base the company's producing properties and gathering facilities and to allow the company, as an operating expense, the fair field value of the gas the company produced. In answering this contention the Court pointed out that the Commission could have used precisely the method urged upon it by the transmission line without changing the result reached in the order under attack. 324 U. S. at 603. For this reason and for the reason that the language of the Act nowhere indicated that Congress intended that the particular method of regulation urged on the Court be used, the Court followed its holding in the *Hope* case that under the Act it is "the result reached not the method employed which is controlling." 324 U. S. at 603.

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[42] Another form of this problem raising the question of the impact of such regulation on the regulatory powers of the producing states is involved in Northern Natural Gas Company, et al. v. Federal Power Commission, Nos. 381 and 382, now pending on a petition for rehearing from a denial of certiorari in this Court.

[43] See also Federal Power Commission v. Natural Gas Pipeline Co., 315 U. S. 575, 584.

The *Hope* and the *Colorado Interstate* decisions flow from the fact that when Congress decided to regulate the interstate service of transmitting gas to consumer markets it necessarily had to regulate companies performing that service regardless of whether they also owned producing properties and gathering facilities. Where such companies are regulated, as the Court pointed out in the *Colorado Interstate* case, the regulation has some necessary impact on the value of those properties and facilities, and it will have that impact regardless of the method of regulation used. This is unavoidable because at the end of interstate transmission the price of natural gas as a mineral is inseparable from the cost of transporting it to the consumer market. But, as the Court also pointed out in the *Colorado Interstate* case, the impact is not a direct one; it is an indirect impact whose effect is to a large extent diluted because the predominant part of the properties comprising the rate base are the transmission properties and not the producing and gathering properties.[44] For the same reason the predominant part of the cost to the consumer is the cost of transportation, not the field value of the gas itself. See *Cities Service Gas Co.* v. *Peerless Oil & Gas Co.*, 340 U. S. 179, 187.

Both decisions recognized, while facing up to the necessary indirect impact of rate regulation on producing and gathering, that the Act was drafted and intended to exclude any direct federal regulation of the producing and gathering business. In the *Hope* case, for example, this Court emphasized that the cut of the legislation was against the transmission company problem, leaving to the states regulation of the business of production and gathering for

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[44] Even so, four Justices of this Court dissented in the Colorado Interstate case on the ground that the Commission's order subjected the company's production and gathering facilities to the same regulation imposed upon petitioner's property used in the interstate transportation and sale of gas for resale, and that this was prohibited by the provisions of the statute (324 U. S. at 615-625).

conservation or other legitimate local purposes. The Court stated (320 U. S. at 610):

> ". . . the bill was designed to take 'no authority from State commissions' and was 'so drawn as to complement and in no manner usurp State regulatory authority.' *Id.*, p. 2. And the Federal Power Commission was given no authority over the 'production or gathering of natural gas.' § 1(b).
>
> "The primary aim of this legislation was to protect consumers against exploitation at the hands of natural gas companies. Due to the hiatus in regulation which resulted from the *Kansas Gas Co.* case and related decisions state commissions found it difficult or impossible to discover what it cost interstate pipe-line companies to deliver gas within the consuming states; and thus they were thwarted in local regulation. H. Rep. No. 709, *supra*, p. 3. Moreover, the investigations of the Federal Trade Commission had disclosed that the majority of the pipe-line mileage in the country used to transport natural gas, together with an increasing percentage of the natural gas supply for pipe-line transportation, had been acquired by a handful of holding companies. State commissions, independent producers, and communities having or seeking the service were growing quite helpless against these combinations. These were the types of problems with which those participating in the hearings were preoccupied. Congress addressed itself to those specific evils."

It is to be noted that in this passage the Court described the "hiatus" in regulation that the statute was intended to close as being a "hiatus" in the authority to regulate the "interstate pipe-line companies" which delivered gas "within the consuming states," a description that recognizes and confirms the plain import of the legislative history. See pp. 38-40, *supra*.[45]

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[45] See also United States v. Public Utilities Commission of California, 345 U. S. 295, 311, where this Court described the pre-statutory gap in terms of a lack of power to control "utility rates" and as a gap in "utility regulation". And see also Panhandle Eastern Pipe Line Co. v. Public Service Commission of Indiana, 332 U. S. 507, 514.

The Court also expressly recognized that the power left in the producing states was the total of its constitutional power over the activities of independent producers and gatherers, that is to say, "those who sell their gas to the interstate operator." The Court said (*id.* 614-615):

> "It is hardly necessary to add that a limitation on the net earnings of a natural gas company from its interstate business is not a limitation on the power of the producing state either to safeguard its tax revenues from that industry or to protect the interests of those who sell their gas to the interstate operator. The return which the Commission allowed was the net return after all such charges."

The case of *Interstate Natural Gas Co.* v. *Federal Power Commission,* 331 U. S. 682, which was heavily relied upon by the Court of Appeals, deals with another form of the rate regulation problem considered in the *Hope* and *Colorado Interstate* cases. In the *Interstate* case, following successful resistance by Interstate of attempts by the State of Louisiana to regulate it, the Federal Power Commission was asked by the State to fix the rates on Interstate's transmission business. 331 U. S. at 687 n. 9; 691 n. 22; 692.[46] In fixing those rates the Commission asserted jurisdiction over the whole of Interstate's business, including three sales made by it in the producing field. Interstate contended that these sales should have been exempt under the production or gathering exemption. In rejecting this contention, the Commission found, in effect, that the sales were part of Interstate's transmission business and not

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[46] Interstate's producing properties and gathering facilities were located in the State of Louisiana. The fact that the State did not oppose federal regulation of Interstate's business was regarded by this Court as persuasive evidence that the Commission's assertion of jurisdiction did not intrude federal power into an area reserved for state action.

exempt as a part of production or gathering. *Interstate Natural Gas Co., Inc.*, 3 F.P.C. 416 at 420, 432-433.[47]

This Court upheld the Commission's assertion of jurisdiction over the sales. In its opinion the Court set forth a test to be applied in determining whether sales made by a transmission company at points physically close to the company's producing facilities and gathering lines are exempt from regulation. This test seems clearly to be based upon regard for the intention of Congress to exclude from federal regulation the business of production and gathering and to leave to the states full freedom to act in that area in the interests of conservation. The test was stated by the Court in the following terms (*id.* 690):

> "Clearly, among the powers thus reserved to the States is the power to regulate the physical production and gathering of natural gas in the interests of conservation or of any other consideration of legitimate local concern. It was the intention of Congress to give the States full freedom in these matters. Thus, where sales, though technically consummated in interstate commerce, are made during the course of production and gathering and are so closely connected with the local incidents of that process as to render rate regulation by the Federal Power Commission inconsistent or a substantial interference with the exercise by the State of its regulatory functions, the jurisdiction of the Federal Power Commission does not attach."

This test gives full effect to the exemption as applied to the operations of the transmission companies which Congress was seeking to regulate. The regulation imposed on Interstate by the Federal Power Commission did not

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[47] The Commission found that the gathering process was completed at some point prior to the sale. See 331 U. S. 682, 692. Physically the sales were made out of Interstate's transmission lines which were in fact the lines by which Interstate carried gas from the producing field to consumer markets. The Commission found that "interstate transportation" in the statutory sense had occurred prior to the sales (3 F.P.C. at 420, 433).

involve any direct regulation of producing or gathering. Interstate itself, as the Commission found, did not treat the challenged sales any differently from the rest of its sales. The rate regulation which the Commission imposed on Interstate allowed a fair return on the whole of Interstate's business, the rates for the challenged sales being set on the basis of an allocation of the reduction in the total return from that business. In setting these rates the Commission allowed as an operating expense the cost of gas purchased by Interstate from companies which produced and gathered it and then sold it to Interstate at the end of their gathering facilities. This Court did not review the fairness of the allocation of the overall rate reduction which was made by the Commission, but the court below upheld it solely on the basis that Interstate was forced to concede that it was getting a fair return on the whole of its business. 156 F. 2d 949, 950-951.

In such a situation, as in the *Colorado Interstate* and *Hope* cases, the rate regulation has no direct impact on the producing properties and gathering facilities. It has the same unavoidable indirect effect on those facilities that the rate regulation in *Hope* and *Colorado Interstate* had. But the rate base on which the return to the company is allowed is a base consisting largely of the cost of transmission and the direct impact of the regulation is on the transmission business and not on the producing and gathering activities of the regulated company. In such a case there is no direct regulation of production or gathering and no necessary or clear invasion of the area reserved to the states.[48] Accordingly, the Court held, the company

[48] In its brief and argument before this Court in the Interstate case, the Federal Power Commission repeatedly called to the attention of this Court the distinction between regulation of sales made at arm's length by independent producers and gatherers and sales made by transmission companies at points physically close to their producing and gathering facilities. Brief for the Federal Power Commission, Interstate Natural Gas Co. v. Federal Power Commission, No. 733, Oct. Term, 1946, pp. 18-19, 34-35, 40-45.

must prove that the sales involved are so inextricable a part of a production and gathering business carried on separately from the transmission business that any regulation of them would necessarily intrude into the area reserved to the states and interfere with the constitutional power of the states to regulate in that area.

The test laid down in the *Interstate* case is appropriate for determining when regulation of an integrated interstate transmission business will directly regulate production or gathering and therefore intrude into the area in which the states are competent to act. But there is no occasion to use the test when the asserted regulation applies to independent producers and gatherers. Such regulation is necessarily regulation of the producing and gathering business and not of the transmission business and must necessarily invade the area of state power. The rate base would consist solely of producing properties and gathering facilities which are admittedly exempt under any construction of the Act.[49] The intrusion into the area reserved to the states would be direct and unavoidable, as is demonstrated by the findings of the Commission in this case and the underlying facts on which those findings are based. See pages 73-84, *infra*. The rate fixed would not be the cost of the transportation service at which the Act is directed, but would be the price of gas as a mineral. It is the price of gas in this sense which has a direct effect on the conservation policies of the producing states and it is the price of the gas in this sense that this Court has held that the producing states may fix for conservation purposes. See *Cities Service Gas Co.* v. *Peerless Oil & Gas Co.*, 340 U. S. 179.

The *Interstate* case therefore is not and cannot be a precedent for any direct regulation of any part of the

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[49] The possibility relied on in the Colorado Interstate case of excluding the producing properties and gathering facilities from the rate base and still reaching the same result would of course be unavailable to the Commission. See 324 U. S. at 603-604.

business of producing and gathering natural gas. In the only instance in which the Commission has attempted such direct regulation this Court struck down the attempt even though it was defended on the ground that it was necessary to adequate regulation of an interstate transmission company clearly engaged in the interstate transmission business which Congress intended to regulate. *Federal Power Commission* v. *Panhandle Eastern Pipe Line Co.*, 337 U. S. 498. In that case the Commission asserted jurisdiction over a proposed transfer of gas leases on the grounds that the transfer might deprive Panhandle of the ability to perform the services for which the Commission had granted it a certificate of convenience and necessity. This Court reviewed the legislative history in detail and concluded that the production or gathering exemption must be given its full scope. The Court, in rejecting the Commission's arguments, said (*id.* 509-513):

> "To accept these arguments springing from power to allow interstate service, fix rates, and control abandonment would establish wide control by the Federal Power Commission over the production and gathering of gas. It would invite expansion of power into other phases of the forbidden area. It would be an assumption of powers specifically denied the Commission by the words of the Act as explained in the report and on the floor of both Houses of Congress. The legislative history of this Act is replete with evidence of the care taken by Congress to keep the power over the production and gathering of gas within the states. This probably occurred because the state legislatures, in the interests of conservation, had delegated broad and elaborate power to their regulatory bodies over all aspects of producing gas. The Natural Gas Act was designed to supplement state power and to produce a harmonious and comprehensive regulation of the industry."

The Court rejected the argument that the *Colorado Interstate* decision was a precedent for direct regulation of the business of production and gathering. In doing so

the Court stated that even though it was apparent that "the cost of gas bought by a natural gas company from producers" would be a weighty factor in rate making, Congress nevertheless excluded the Commission "from exercising any direct control or regulation over the actual production and gathering of gas." After describing its holding in the *Colorado Interstate* case the Court went on to say (*id.* at 506-507):

> "The use of such data for rate making is not a precedent for regulation of any part of production or marketing. Before the *Colorado Interstate* decision, it was apparent that the value of producing facilities and the cost of gas bought by a natural-gas company from producers would be weighty factors in rate making whether a rate-base method or other method for fixing rates was used. Low valuation by the Commission of producing properties or low-cost allowance for purchased gas discourages exploration for gas or its sale in interstate commerce. Congress knew this necessary relationship between production and distribution but excluded the Commission from exercising any direct control or regulation over the actual production and gathering of natural gas."

II

THE DECISION OF THE FEDERAL POWER COMMISSION THAT PHILLIPS' SALES ARE NOT SUBJECT TO FEDERAL REGULATION BECAUSE THEY ARE PART OF THE BUSINESS OF PRODUCING AND GATHERING IS CORRECT IN LAW AND FACT AND SHOULD BE UPHELD

A. THE COMMISSION CORRECTLY CONSTRUED THE NATURAL GAS ACT TO EXCLUDE THE WHOLE OF THE BUSINESS OF PRODUCING AND GATHERING

In its opinion in this case, the Commission noted that in addition to making an analysis of the record and briefs before it, it also made "an extensive review of the provisions of the Act, its history, our own decisions during 13 years of administering the Act, and relevant judicial decisions" (R. 1741). From that analysis and review the Com-

mission concluded again, as it had in prior cases, that it had no jurisdiction over transportation or sales made as a part of production and gathering. It construed the meaning of the words "production or gathering" in Section 1(b) of the Act in the following terms (*ibid.*):

> "We believe that Congress, by the exemption of production and gathering, intended to deny this Commission jurisdiction over the business of producing and gathering."

In the preceding sections of the brief we have shown that this construction of the statute is correct as a matter of law. A reading of the words of the statute in their ordinary sense shows that the Act contemplates only regulation of interstate transmission companies performing the service of transporting gas to consumer markets. The legislative history taken as a whole confirms that this is the meaning of the statute and that Congress did not intend to intrude federal regulation in any degree into the areas of local concern at either end of the business of transporting gas interstate to consumer markets. The exclusion from regulation of "production or gathering" should therefore as a matter of statutory construction be taken to mean that no direct regulation of any part of the business of production and gathering is authorized by the Act. This construction of the statute has been followed by the Commission during the 16 years since the passage of the Act and the principles on which it rests are reflected in the decisions of this Court.

On this construction of the statute Phillips' sales are immune from regulation unless it can be said that the sales, viewed in terms of business operations and economic function, are not a part of the business of producing and gathering. The Commission considered this point and found that in fact Phillips' sales were made as a part of the business of production and gathering; this finding was fully supported by the evidence. See pp. 67-72, *infra*.

Although there are passages in the opinion of the court below that show that the court rejected the Commission's appraisal of the facts, the court did not purport to set aside this finding by the Commission on the ground that it was unsupported by the evidence or erroneous in fact. The court rather took the position that the case turned on a question of law. In the concluding paragraph of its opinion it stated that the validity of the Commission's decision was "not dependent upon the evaluation of testimony or upon any facts peculiar to this case" and that the Commission "has applied an erroneous rule of law" (R. 1849).

The court below did not attempt a definition of the statutory phrase "production or gathering" or otherwise explain the scope that it believed the phrase might properly be given. Consequently neither the court's interpretation of the statute nor the reasons for that interpretation are entirely clear. There is no doubt, however, that the court construed the words "production or gathering" as covering something less than the whole of the business of an independent producer and gatherer. In thus limiting the meaning of those words the court below erred.

In part, the holding of the court below appears to be based on its conclusion that in the circumstances of this particular case Phillips' sales were preceded by activities that could not as a matter of law or fact be considered a part of "production or gathering" within the meaning of the Act; this appears to be the significance of the court's statement that the sales were made after processing had "intervened" and after the gas had moved through short plant outlets (R. 1842). As is pointed out below, there is no basis in either law or fact for this conclusion and the court committed error in relying on it. See pp. 70-73 *infra*.

At the same time, it seems clear that the court did not intend to rest its decision solely on this limited basis. The ultimate premise of its opinion appears to be a more basic construction of the statute. The Court stated broadly

that the "exemption of production or gathering does not exempt sales made after production and gathering have been completed" and that the exemption does not cover "interstate sales of gas by the corporation that produced and gathered it" (R. 1849). These statements, read in the light of the court's assertion that nothing turned "upon any facts peculiar to this case" (*ibid.*), seem to mean that the Court of Appeals construed the words "production or gathering" as not covering sales made as the final and culminating step in the gathering process.

There is nothing anywhere in the statute which in any way lends support to a construction of the words "production or gathering" which is limited in this respect. The statute speaks in terms of whole segments of the industry. Section 1(a) defines the business covered by the statute as the business of transportation and sale of natural gas in interstate commerce. Section 1(b) specifically excludes the areas at either end of this business—"local distribution" and "production or gathering"—and does so in generic terms without limitation. Nothing in the regulatory provisions of the statute which follow, such as the provisions giving the Commission authority to fix rates, prevent abandonment and issue certificates of convenience and necessity, in any way detracts from the broad statement of affirmative coverage and the generic descriptions of the exempted areas which are contained in Section 1. Compare *Federal Power Commission* v. *Panhandle Eastern Pipe Line Co.*, 337 U. S. 498, 507-509.

For these reasons the court's construction of the words "production or gathering" must rest on some ground that does not appear on the face of the statute. That ground is disclosed in the court's discussion of the constitutional powers of the states to regulate field sales of natural gas. The court stated that in its opinion no state could regulate Phillips' sales and distinguished this Court's opinion in *Cities Service Gas Co.* v. *Peerless Oil & Gas Co.*,

340 U. S. 179, on the ground that unlike the sales there involved, Phillips' sales are made "after the gas has been gathered into trunk lines" (R. 1847). The court below, however, apparently considered that sales in interstate commerce at the well-head were exempt from regulation under the Act. This discussion of the constitutional powers of the states, read in connection with the court's discussion of legislative history, indicates the basis for the court's conclusion that the words "production or gathering" do not comprehend sales for resale in interstate commerce made as the final and culminating step in the gathering process. The court apparently believed that the states have no constitutional power to regulate such sales and that since the Act was intended to fill a gap in regulation it necessarily follows that federal authority extends to all such sales.

In accepting this argument as a basis for its construction of the statute, the court below did not go so far as to hold that all sales for resale in interstate commerce are subject to federal regulation because no state can regulate them in the same manner as they are regulated under the Natural Gas Act. Indeed the court below could not have taken that position in view of this Court's statement in *Interstate Natural Gas Co.* v. *Federal Power Commission*, 331 U.S. 682, 690, to the effect that even in the case of an interstate transmission company sales for resale in interstate commerce may be exempt from federal regulation under the production or gathering exemption if federal rate regulation would interfere with state conservation power as distinguished from state power to impose the kind of regulation provided for by the Natural Gas Act.[50]

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[50] In view of the opinion in the Interstate case it is unnecessary to consider the extent of power of the states to regulate for purposes other than conservation. However, the constitutional principles reaffirmed by this Court in the Cities Service case would permit a producing state to regulate interstate sales for the pur-

The position adopted by the Court of Appeals is more restricted. This position is that Congress meant by the Natural Gas Act to grant authority to the Federal Power Commission to regulate all sales for resale which could not constitutionally be regulated by any state for any purpose. In its opinion, for example, the court apparently thought that sales for resale in interstate commerce made at the well-head fell within the exemption of "production or gathering" because under this Court's decision in *Cities Service Gas Co.* v. *Peerless Oil & Gas Co.*, 340 U.S. 179, the producing states have the power to fix minimum prices on such sales in aid of conservation (R. 1847).

This position involves both a misinterpretation of the legislative history and an erroneous view of the scope of state power. So far as concerns legislative history, it is clear that the "gap" with which Congress was concerned was a "gap" in the power of the consuming states to regulate the companies performing the service of transporting gas interstate to consumer markets. The gap that Congress closed was not related to the activities of independent producers or gatherers and was not conceived in terms of the constitutional power of the states to regulate those activities. See pp. 38-40, *supra*.

In any event, there is nothing in the *Cities Service* case nor in the decisions on which it relies which would distinguish between sales made at the well-head and sales such as Phillips' which are made at the end of gathering.[51] The test of the constitutional competence of the

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pose of protecting consumers if it could be shown that the regulation did not discriminate against interstate commerce, was designed to protect a legitimate state interest, and that the local interest to be served outweighed whatever national interest there might be against state restrictions. These questions could only be resolved by this Court on a case-to-case basis. Prudential Insurance Co. v. Benjamin, 328 U.S. 408.

[51] The Court of Appeals also quoted the language from the opinion of this Court in Federal Power Commission v. East Ohio Gas

states to regulate sales in aid of conservation is a practical test, not a mechanical test. It does not depend upon the physical point in the producing fields at which the sales are made, but rather upon the relationship between the sales and the states' interest in the price of gas as a factor in conservation policy. Under this test it is clear that the states do have the constitutional power to regulate sales such as Phillips' in aid of conservation.

The *Cities Service* case specified three criteria against which the constitutionality of state regulations having an impact on interstate commerce are to be tested. These three criteria are that the regulation not discriminate against or place an embargo on interstate commerce, that it safeguard an obvious state interest, and that the local interest at stake outweigh whatever national interest there might be in the prevention of state restrictions (340 U.S. at 186-187).[52] No question of discrimination or an embargo would be raised by regulation of Phillips' sales.

Co., 338 U.S. 464, 472, to the effect that the gap closed by the Act is to be measured by the status of constitutional law at the time of the passage of the Act, and not by its present status. The apparent purpose of the Court of Appeals' statement was to indicate doubt that the Cities Service case would have been decided the same way prior to 1938. There is no merit in the suggestion of the Court of Appeals. For one thing, it is clear from the context of the East Ohio case that this Court was speaking of the power of consuming states to impose utility-type regulation on transmission companies. In addition, as we have pointed out above, the Cities Service case rests on principles preceding the Natural Gas Act by decades. See note 32, pp. 40-41.

[52] These criteria may be compared with the tests applied to determine the validity of state taxation measures under the commerce clause. See for example Michigan-Wisconsin Pipe Line Co. v. Calvert, Nos. 198-201, this Term, 22 U. S. Law Week 4115 (February 8, 1954); and see Freeman v. Hewit, 329 U. S. 249, 252-253. The decision in the *Michigan-Wisconsin Pipe Line Company* case held invalid a Texas tax levied on the taking of natural gas by two of the interstate transmission companies supplied by Phillips. Because of the differences in the issues involved and because the

The "legitimate local interest" which is at stake in the case of Phillips' sales is precisely the same as in the *Cities Service* case. The balancing between the local interest and the national interest depends upon a number of factors which are specified and discussed in the *Cities Service* case. These factors, which are set forth in the following paragraph of the Court's opinion, apply to sales at the end of gathering to the same degree as they apply to sales at the well-head. The Court stated (340 U.S at 187-188):

> "We recognize that there is also a strong national interest in natural gas problems. But it is far from clear that on balance such interest is harmed by the state regulations under attack here. Presumably all consumers, domestic and industrial alike, want to obtain natural gas as cheaply as possible. On the other hand, groups connected with the production and transportation of competing fuels complain of the competition of cheap gas. Moreover, the wellhead price of gas is but a fraction of the price paid by domestic consumers at the burner-tip, so that the field price as herein set may have little or no effect on the domestic delivered price. Some industrial consumers, who get bargain rates on gas for 'inferior' uses, may suffer. But strong arguments have been made that the national interest lies in preserving this limited resource for domestic and industrial uses for which natural gas has no completely satisfactory substitute. See generally, Federal Power Commission, Natural Gas Investigation (1948); *Federal Power Comm'n* v. *Hope Natural Gas Co.*, 320 U.S. 591, 657-660 (1944) (dissenting opinion). Insofar as conservation is concerned, the national interest and the interest of producing states may well tend to coincide. In any event, in a field of this complexity with such diverse inter-

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tax was levied on the interstate transmission companies and not on the operations of Phillips, the decision is not directly relevant here. It should be noted, however, that in deciding that case the Court distinguished between Phillips' local activities of production, gathering and processing on the one hand and the predominantly interstate function of the transmission companies on the other.

ests involved, we cannot say that there is a clear national interest so harmed that the state price-fixing orders here employed fall within the ban of the Commerce Clause. *Parker* v. *Brown, supra; Milk Control Board* v. *Eisenberg Farm Products, supra.* Nor is it for us to consider whether Oklahoma's unilateral efforts to conserve gas will be fully effective. See *South Carolina Highway Dept.* v. *Barnwell Bros., supra* at 190-191."

This Court itself has recognized that to be effective, regulation of the kind upheld in the *Cities Service* case cannot be confined to sales at the well-head but must extend to sales made elsewhere in the producing field. In *Phillips Petroleum Co.* v. *Oklahoma,* 340 U.S. 190, 192, this Court pointed out that "in a field which constitutes a common reservoir of gas" the state "must be able to regulate the operations of all producers or there is little point in regulating any."[53] The Corporation Commission of the State of Oklahoma construed the order involved in the *Cities Service* case as not confined to transactions at the well-head but as also prescribing a price to be realized in sales made during or upon the conclusion of gathering.[54]

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[53] This case involved the application to Phillips' activities in the Guymon-Hugoton Field (including the transactions with Panhandle Eastern Pipe Line Company which are involved in the instant case) of the Oklahoma order upheld in the Cities Service case. The attack on the order was based solely on the due process clause of the Fourteenth Amendment; the question of the validity of the order under the commerce clause, which was raised in the Cities Service case, was therefore not before the Court in the Phillips case.

[54] The order of the Corporation Commission of Oklahoma construing its regulation as applicable to Phillips' operations in the Guymon-Hugoton Field, even though Phillips did not sell gas at the wellhead but sold after gathering and processing, appears in the Record (Ex. 120A; R. 1277-1283).

The order of the Corporation Commission now in effect reads in part as follows (Order No. 26906, issued August 8, 1952):

"1. That no gas shall be produced from any well located in the Guymon-Hugoton Field of Oklahoma except at a price of

The opinion of the Court of Appeals in this case seems to rest on the belief that to the extent that any state regulatory order of this kind applies to sales made at the end of gathering, the order is unconstitutional. The *Cities Service* case makes it clear that this belief is erroneous. This error is crucial to the court's conclusion that sales made at the end of gathering are subject to federal regulation; on the court's reasoning, that result followed only because the states have no power to regulate the sales for any purpose. Hence even if we accept *arguendo* the court's construction of the statute, its conclusion that sales made as the culminating step in gathering are subject to federal regulation is wrong because that conclusion rests on a basic error as to the extent of state power.

B. THE COMMISSION CORRECTLY FOUND THAT PHILLIPS' MOVEMENT, PROCESSING AND SALES OF NATURAL GAS ARE ALL A PART OF THE BUSINESS OF PRODUCING AND GATHERING

The Commission's ultimate finding of fact on the nature of Phillips' business follows (R. 1742):

> "The facts of this case convince us that we have no jurisdiction over Phillips. We find that its operations, so far as relevant, consist of production and

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not less than 9.8262¢ per thousand cubic feet if sold at the wellhead or on the lease or drilling unit from which produced, or a price equivalent to not less than 9.8262¢ per thousand cubic feet at the wellhead if sold off the lease or drilling unit or otherwise utilized. If the gas is sold during or upon conclusion of gathering without being processed for the extraction of liquid hydrocarbons, the price shall be not less than 9.8262¢ per thousand cubic feet plus the reasonable cost of gathering. If the gas is processed for extraction of liquid hydrocarbons and sold during or at the conclusion of gathering, the price for the residue gas shall be not less than 9.8262¢ per thousand cubic feet."

As a basis for this order the Corporation Commission of Oklahoma found: "That only a small portion of the gas produced in said Field [Guymon-Hugoton] is actually sold or delivered at the wellhead * * *"

gathering, or incidents of or activities related to these functions thus requiring their inclusion within the Act's exemption."

This finding of fact rests upon the Commission's careful appraisal of all relevant aspects of Phillips' activities. The Commission took into account the pattern and characteristics of the lines (including their length and size) by which the gas is brought to the point of final commingling in the processing plants; the character and purpose of the processing; the physical relationship between the gathering, the processing, and the delivery and sale to the interstate transmission line; and the economic relationship existing between all of Phillips' activities, including the sales, and the business of producing and gathering gas.

The evidence established, beyond controversy, that Phillips' gas business consists solely of the following operations: Phillips produces gas and buys it from other producers; it collects the gas, so produced or purchased, by systems of converging pipe lines, in plants where the gas is commingled and processed to remove impurities and liquid hydrocarbons. Part of the gas is then returned by Phillips to producers from whom it was originally bought, part is sold for local use, and part is sold to the interstate transmission companies. The gas sold by Phillips to the interstate transmission companies is delivered to those companies through short pipe outlets or exhausts that carry the gas to points within or at the borders of the yards of Phillips' processing plants. All of these activities are carried on in the producing fields. Phillips does not own or operate an interstate transmission line and is not affiliated with any company that does.[55]

These facts alone were sufficient to support the Commission's finding that all of Phillips' activities, including its sales to the transmission companies, were a part of the

[55] No serious contention was made before the Commission or in the court below that Phillips was an interstate transmission company in the sense of being engaged in the business of transporting gas from the producing fields to consumer markets.

business of producing or gathering. In addition, however, the Commission's finding was supported by evidence, given by witnesses experienced in the oil and gas industry, with respect to what "production or gathering" comprehends in terms of business practices and economic function.[56]

That evidence covered all stages of Phillips' gas activities, including its sales to the transmission companies. There was proof that all of Phillips' lines were regarded by those who operated them in the field, and by the industry generally, as gathering lines and as constituting gathering systems (R. 146-148, 190, 205-206, 270-273, 364-374, 644-672). There was testimony that gathering comprehends both the collection of gas from wells to a point or points in or near the field and the preparation or processing of the gas for market; that historically it has been the practice in the oil and gas industry for independent producers and gatherers to process gas as a part of their business; that Phillips had been processing gas as a part of its gathering business since 1921, and that Phillips' processing facilities have always been classified by Phillips, and regarded in the industry, as a part of its gathering systems (R. 311-315, 364-369, 691). There was also evidence that gathering was conducted for the specific purpose of disposing of the gas, whether by use or sale (R. 310-311, 324-325, 368-369, 691-692, 699-701, 701-702), and that sale at the processing plant was a part of gathering (R. 636, 677).

The Commission's findings embody the considered judgment of the administrative agency authorized by Congress to apply the general words of the statute to particular situations. The findings have a reasonable basis in law and are supported by substantial evidence. Under well established rules of judicial review they should be

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[56] It was proper for the Commission to receive and to be guided by evidence of this kind. See O'Hara v. Luckenbach S. S. Co., 269 U.S. 364; United States v. Maher, 307 U.S. 148, 155; Order of Railway Conductors v. Swan, 329 U.S. 520, 525; Carter v. Liquid Carbonic Pacific Corporation, 97 F. 2d 1 (9th Cir. 1938); Roberts v. Tennessee Coal, Iron & R. Co., 255 Fed. 469 (5th Cir. 1919), cert. denied 250 U.S. 659.

accepted by the courts.[57] *Gray* v. *Powell*, 314 U.S. 402, 413; *United States* v. *Wabash R. Co.*, 321 U.S. 403, 408; *Cardillo* v. *Liberty Mutual Co.*, 330 U.S. 469; *National Labor Relations Board* v. *Hearst Publications, Inc.*, 322 U.S. 111, 130-131; *Unemployment Compensation Commission of Alaska* v. *Aragon*, 329 U.S. 143, 153-154.

In the court below the Commission's findings were attacked on the ground that because of the special or peculiar nature of certain of Phillips' operations the Commission could not properly find that those operations were part of production or gathering. As has been seen, the Court of Appeals purported to dispose of the case on a basis that did not require it to consider these attacks on the Commission's findings. It nevertheless appears that the court below, in addition to misconstruing the statute, accepted certain of the attacks made on the Commission's findings.

In holding that Phillips' sales were made after production and gathering were "complete" the court below said (R. 1842):

> "Thus Phillips sells the gas after the time and beyond the place at which production and gathering are complete and after processing has intervened. For example, gas processed in one Phillips plant then flows about 240 feet through a Phillips pipeline to sales meters owned and operated by Phillips, where it is sold and delivered to Panhandle Eastern Pipe Line Company."

In this passage the court below first assumes that processing cannot be a part of the business of producing or gathering and then rests its conclusion that Phillips' sales were made after production and gathering were "complete" at least in part on that assumption. Similarly, the court, although not explicitly holding that the movement of the gas for 240 feet through the plant outlet is interstate transpor-

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[57] Section 19(b) of the Natural Gas Act provides that on judicial review "The findings of the Commission as to the facts, if supported by substantial evidence, shall be conclusive."

tation in the statutory sense, regarded this movement as not being part of production or gathering.

In another portion of the opinion, the court below rejected the Commission's findings on the nature of the lines by which Phillips moves gas into its processing plants. To support its conclusion that Phillips' sales are not subject to any kind of regulation by the producing states the court below cited *Federal Power Commission* v. *East Ohio Gas Co.*, 338 U.S. 464, for the proposition that when the Natural Gas Act was passed it was established that state regulatory power could not reach "high pressure trunk lines". In a footnote the court went on to observe that Phillips' sales, unlike the sales in *Cities Service Gas Co.* v. *Peerless Oil & Gas Co.*, "are made after the gas has been gathered into trunk lines" (R. 1847). The words "high pressure trunk lines" were used in the opinion in the *East Ohio Gas Co.* case to describe the interstate transmission lines that carry gas from producing fields to consumer markets. It is therefore difficult to avoid the conclusion that in this passage the court below, contrary to the findings of the Commission, determined that all of the lines leading into the processing plants are not gathering lines but are in all significant respects just like interstate transmission lines.[58] The disregard of the Commission's findings in this instance is of particular importance because it lies at the base of the argument on constitutional law by which the court below supported its construction of the statute.

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[58] It is not clear whether the court below meant to determine as a fact that Phillips' lines were "high pressure" lines. If so, the determination disregards the findings in the Commission's opinion with respect to the pressures in the different lines. The record does not disclose any pressures in the lines leading into the processing plants which could be described as "high". In fact the findings and the record show that much of the gas moves through the lines and the processing plants at well-head pressure (R. 1692, 1695, 1706).

In these instances the court below improperly disregarded the Commission's findings of fact. To the extent that the court was assuming to decide these questions as a matter of law it was acting on an erroneous construction of the statute. The words "production or gathering" describe a business or economic function. Whether the words cover particular processing activities, particular movements of gas, or particular pipe lines, depends upon the relationship existing between the processing, the movements, or the pipe lines, and the business or function described by the statutory word. The determination of that relationship turns on questions of fact, not questions of law.[59]

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[59] For example, to say broadly that as a matter of law processing can never be a part of production or gathering would disregard the realities of the oil and gas business. Natural gas must be processed if it is to be effectively and economically used. In the historical development of the industry it was normal for the person who produced and gathered to do the necessary processing and to sell the residue gas as a part of his business (R. 365-366). In the FTC Report (p. 115) it was noted that the practice had grown up of "scrubbing or washing the gas at important gathering centers in the field whereby certain amounts of so-called 'natural gasoline" are recovered and sold, and any dirt, dust and water vapor are removed." The report also pointed out that the extraction of by-products from natural gas was performed both by producing interests and by transmission interests (*id.* 55).

The functional status of processing is a question to be decided on the facts of particular cases. In some cases, as here, it is a part of the business of producing and gathering. In other instances processing may be a part of the business of an interstate transmission company. In others it may be unrelated to either the business of producing or gathering, or the business of interstate transmission.

Similarly, since all interstate movement is not "transportation" in the statutory sense (see pp. 25-26, *supra*), the determination whether particular movement is a part of gathering must be based on an appraisal of the relevant facts. It is the duty of the Commission to determine in each case in which the question arises at what point in the interstate movement of gas "gathering" ends and "transportation" in the statutory sense begins.

Congress intended that the Commission should decide these questions of fact as they arise in particular cases on the basis of all of the relevant facts. Such questions are peculiarly matters that require the exercise of the "expert, experienced judgment" of the regulatory agency. Compare *Gray* v. *Powell*, 314 U.S. 402, 413. In this proceeding the Commission carefully exercised that judgment. It determined on all the facts that Phillips' processing and the movement of gas to the plant outlets were both part of the business of production and gathering (R. 1743). Similarly, it found that all of the lines leading to the processing plants were gathering lines forming a part of Phillips' gathering business and were not transmission lines. To the extent that the court below rejected these findings and substituted its own determinations of fact, it committed error which vitiates its conclusions of law.

III

The decision of the Federal Power Commission that sales such as those of Phillips are not subject to federal regulation is confirmed by its finding that its regulation of such sales would be inconsistent with state conservation programs

The Commission's decision in this case rested in the first instance, as we have seen, on its holding that the Natural Gas Act does not authorize federal regulation of the business of producing and gathering and on its finding of fact that Phillips' sales were made as a part of the business of producing and gathering. In addition, however, to the evidence relating to the nature of Phillips' operations the Commission also received evidence bearing on the relationship between federal regulation of the sales of independent producers or gatherers and state regulatory measures and policies. On the basis of that evidence the Commission found that regulation of sales such as those of Phillips would lead to a substantial interference with the regulatory functions of the producing states (R. 1745).

This finding, although not necessary to support the Commission's decision that Phillips' sales were not subject to federal regulation, confirms the grounds on which the decision rests.[60]

In the consideration of the legislative history we have seen that Congress did not intend to subject to federal regulation any part of the business of independent producers and gatherers. Congress was concerned solely with evils found to exist in the conduct of the business of transporting gas interstate from producing fields to consumer markets. But, even in the regulation of the interstate transmission business, Congress was careful to provide that the statute should not apply to production or gathering. It did this because it recognized that any direct regulation of production or gathering would extend federal authority into an area in which its exercise would interfere with the legitimate regulatory functions of the states. See *Interstate Natural Gas Co.* v. *Federal Power Commission*, 331 U. S. 682, 690. The Commission's finding that federal regulation of field sales by independent producers and gatherers would interfere with these state functions shows that extension of federal authority to those transactions would necessarily create the conflict which, even in the regulation of the interstate transmission companies, Congress intended to avoid. The finding, therefore, together with the evidence that supports it, shows that Congress could not have intended to provide for federal regulation of sales such as those of Phillips.

Much of the evidence that supports the Commission's finding was presented by the intervening states of Oklahoma, Texas and New Mexico and was provided in large part by the testimony of members of the regulatory agen-

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[60] In its opinion the Commission introduced the subject of interference with state regulatory functions by saying: "In addition to the conclusions we have already reached, the evidence in this case supplies still another type of barrier to our regulation of Phillips' sales" (R. 1745).

cies of those states.[61] The nature of the evidence is disclosed by the Commission's findings (R. 1746-1747):

> "In varying degrees, the evidence clearly shows that our regulation of sales made in the process of production and gathering would, by its very nature, be inconsistent or constitute a substantial interference with such regulation of producers and gatherers by Oklahoma, Texas, and New Mexico. To cite one example, there is a direct relation between price and conservation, an important concern in the regulation of each of the States. Even though a producer be allowed a reasonable return on actual legitimate investment, our fixing of maximum rates for his sales would run counter to State conservation efforts, through the fixing of minimum well-head prices or otherwise, to insure maximum recovery of gas prior to abandonment of the well. For the higher the profit, the longer it is economical to operate the well. And to the extent that the producer could obtain a profit higher than that permissible under our maximum-price regulation, the longer abandonment would be postponed. Similarly, the higher the price paid to the producer and gatherer, the easier it becomes for the State to discourage by regulation the flaring of gas and to encourage the gathering and marketing of such gas. This is particularly true as to casinghead gas."

This conclusion that federal regulation would by its very nature be inconsistent with the state programs is supported by substantial evidence. It represents the position of all of the agencies directly concerned—the Federal Power Commission, the agency that would administer and enforce federal regulation, and the regulatory bodies of Oklahoma, Texas and New Mexico. The state regulatory

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[61] Among the witnesses were W. J. Murray, member of the Railroad Commission of Texas, Jack K. Baumel, Chief Engineer of the Texas Commission; Richard R. Spurrier, New Mexico State Geologist and member of its Oil Conservation Commission; Ray C. Jones, member of the Oklahoma Corporation Commission; and Elmer Capshaw, the Oklahoma Commission's Petroleum and Natural Gas Engineer (R. 375-592, 602-619).

authorities and the Commission, all experienced in the industry and familiar with the respective character and purpose of state and federal gas regulation, are best qualified to measure the consequences that would follow the extension of Commission authority to cover Phillips' sales.

As the record shows, Texas, Oklahoma and New Mexico have comprehensive programs covering the production and gathering business to prevent waste of natural gas and to encourage efficiency in its production. It is by such programs, designed to recover the maximum amount of gas (and oil) from the fields, that the states "can assure for the longest period of time an abundant supply to the consumers and at the lowest price" (R. 435). In short, the programs are based on the long-term common interest of both consumers and producers in conserving a nonreplaceable wasting resource (R. 428-430, 436, 459-460).

The programs vary in some aspects, reflecting the individual state's decisions as to the measures best suited for its particular problems. Each state's regulatory pattern, however, includes such conservation measures as proration, allocation and interconnection of wells; unitization, in which a common pool is drilled and operated as a unit; requirements as to well spacing; avoidance of premature abandonment of wells; full exploitation of marginal acreage; maximum utilization of casinghead gas; and bans against flaring or other improper uses of gas.

As the state officials emphasized, the effectiveness of these measures depends on a satisfactory level of field prices for natural gas. The record reveals that the price realized for gas in the producing fields has a direct, immediate and potent effect on conservation.[42] All phases of the state programs, starting with the initial problem of stimulating exploration and drilling to increase gas reserves, are affected by what prices are received by the producer and gatherer in the field. If gas is priced too low,

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[42] R. 429-431, 438-440, 442-448, 454-455, 457-459, 513, 516-519, 523-526, 532, 546-549, 552-553, 559-560, 566, 604-607, 609-614.

exploration is discouraged (R. 459, 517, 529-530, 569). The same direct relationship between the effectiveness of the state conservation programs and the price of gas was shown to exist at other stages of the business of production and gathering. Adequate financial incentive is essential if producers and gatherers are to discover, develop, produce and gather natural gas in ways avoiding physical and economic waste.

The ways in which federal regulation of prices for gas in the field would interfere with the various state measures can be briefly illustrated.

All three states have unitization programs. Under these programs all or a large portion of a common pool is operated as a unit, regardless of the number of owners of interests in the pool. In this way, maximum recovery of oil and gas can be realized. Oklahoma has a compulsory field unitization law.[63] Texas and New Mexico regulations provide for voluntary agreements for unit operation.[64] In both Oklahoma and Texas one of the legal requirements for unitization is that the value of the additional oil and gas to be recovered must exceed the added cost of that method of operation.[65] Thus, the price to be received for the gas may alone determine whether unitization of a particular field will be effected. If the Federal Power Commis-

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[63] Oklahoma Stat. Tit. 52, §§ 287.1-287.15 (1951). An earlier version of this statute was upheld in Palmer Oil Corp. v. Amerada Corp., 343 U.S. 390.

It was under this authority that the Oklahoma Corporation Commission ordered the establishment of the West Edmond Hunton Lime unit in which Phillips, as a member of the unit, is the owner of an undivided interest in the gas sold by the unit to Cities Service. See p. 9, *supra*.

[64] Vernon's Civil Stat. of Texas (1925), Art. 6008b; New Mexico Stat. (1951 Supp), § 69-213½(e), §§ 8-1138, 1139. See also Rule 507 of New Mexico Oil Conservation Commission.

[65] Oklahoma Stat. Tit. 52, § 287.3 (1951); Vernon's Civil Stat. of Texas (1925), Art. 6008b, § 1.

sion should regulate the price received by independent producers and gatherers, the price set by the Commission—fixed by an agency operating under a statute in no way related to conservation interests—could by itself determine whether unit operation of particular fields would be possible.

In no area is the relationship of price to conservation of gas more strikingly apparent than in the instance of casinghead gas, which is produced only as and when oil is produced. Unless casinghead gas is gathered and marketed immediately, it is lost either by flaring or by being allowed to escape. Billions of cubic feet have been so wasted.[66] The extent to which the gas will be gathered and utilized relates most directly to the price for gas, for utilization of casinghead gas involves considerable expense. The gas comes from oil wells that are often widely dispersed and it is usually produced in small volume at each well. Expensive processing is frequently necessary to separate the gas from the oil. Consequently, extensive gathering systems are required to link together the wells and collect and process the gas (R. 387-390, 445).

The states have made substantial progress in reducing the wastage of casinghead gas. In Texas alone, approximately three billion cubic feet per day which formerly would have been wasted are now utilized (R. 389-390). The success of these state efforts is dependent on prices for gas that will make operations to utilize casinghead gas economically feasible (R. 438, 449, 451).

Similarly, other devices designed to insure high recovery of gas in the field, such as well spacing and the prevention of premature abandonment of wells, are basically affected by the price of gas (R. 515-516, 566, 606, 609-610,

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[66] As recently as 1945 a fifth of the Nation's total production of gas was blown away in the air or burned at the well-head. Natural Gas Investigation, Federal Power Commission, Docket G-580, Report of Commissioners Smith and Wimberly (United States Government Printing Office 1948) p. 114.

618-619). As the state officials emphasized in the Commission proceedings, their agencies are acutely aware of the physical and economic waste that occurs when prices for gas are inadequate to permit the effective operation of these and other conservation methods, and recognize that the effectiveness of their programs is basically dependent on the prices realized in the field (R. 431, 458, 524-525, 547-549).

Up to now, the States of Texas and New Mexico have not found it necessary to fix minimum prices in the field. Their present policy is to permit field prices of gas to be fixed by competition rather than by regulation (R. 426-427, 431, 457-461, 464-465, 556-557). Oklahoma, however, has fixed the minimum field prices to be received by producers as a condition to the production of gas in the Guymon-Hugoton Field (Exs. 119, 120, 120A; R. 1246-1283). See pp. 66-67, *supra*. If Texas or New Mexico determines that competitive forces do not result in prices which will permit the realization of their conservation objectives, these two states could adopt price regulation comparable to that now enforced by Oklahoma.[67]

Federal regulation of the field prices received by companies such as Phillips would necessarily conflict with the price programs, policies and regulatory measures of the producing states. If, as in the case of Oklahoma, a state exercised its right to fix minimum prices in the producing field, the assertion of federal power over the same subject matter would create a situation in which two different regulatory agencies would be attempting to regulate the

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[67] The evidence is that the New Mexico Commission now has such power (R. 532). Both New Mexico and Texas have common purchaser statutes authorizing their respective commissions to require mandatory taking and purchasing of gas in connection with proration. New Mexico Stat. (1951 Supp.) § 69-214(b); Vernon's Civil Stat. of Texas (1925), Art. 6049a, §§ 8, 8a, 8aa and 8b. See R. 457. The Oklahoma price orders sustained in the Cities Service case were grounded on essentially the same kind of statutory provision.

same transactions. But even if the states should not assert their power to fix minimum field prices, as is now true of Texas and New Mexico, federal regulation of field prices would still conflict with state power and with programs and policies adopted by the states.

As we have seen, Texas and New Mexico have adopted regulatory policies under which measures for the conservation and efficient production of gas have been developed on the basis of prices set in the field by competitive factors. These two states have decided that the free play of competitive forces will produce a price level that will encourage producers and gatherers to develop gas reserves and to minimize waste (R. 426-427, 431, 457-461, 464-465, 556-557). Federal regulation of prices in the producing fields of these two states would substitute a regulated price level for this competitive price level which the two states have determined is best adapted to protect their legitimate interests in conserving natural gas. In addition, such regulation would necessarily conflict with the power of the states to change their policies and adopt price orders such as Oklahoma has promulgated.

Although it thus appears that the producing states to some degree follow different policies toward field prices the primary concern of all of them lies in the conservation of natural gas. The rate-making standards which the Natural Gas Act establishes to guide the Federal Power Commission in the exercise of its authority do not take these conservation interests into account. The Commission itself recognized this fact in its opinion and adverted to the contrast between its statutory duty "to limit rates to an amount sufficient to recover costs plus no more than a reasonable return on actual legitimate investment" with the quite different interests of the producing states in conservation policies and programs (R. 1745-1746).

The various aspects of the state programs, briefly summarized above, have been evolved within a framework in which prices, determined in the case of Oklahoma by ex-

plicit minimum price order and in the case of Texas and New Mexico by competitive forces, are at levels at which increasingly effective conservation programs have been evolved. To replace these price levels with rates determined under the standards established by the Natural Gas Act—designed as we have seen for different purposes and based on other standards—would necessarily disrupt the state programs.

In addition to the interference which would result from the imposition of federal regulation because of the basic importance of price to the effectiveness of the state programs, Federal Power Commission regulation of Phillips' sales or other aspects of producing and gathering operations would be disruptive in still another vital respect. Various aspects of the state conservation programs depend for their effectiveness on maintenance of maximum freedom in the interchange of gas among producers and the continuing cooperation of producers in the states' efforts to promote the efficient use of gas and to prevent waste. Federal regulation would seriously interfere with these state programs.

For example, proration programs, one of the basic conservation devices utilized by all three states, would be handicapped. Under the proration statutes, the state regulatory agency fixes, on the basis of market demand, the amount of production that will be allowed in a field in a particular period.[68] Each producer is given "an allowable", which is his prorationed share of the total production. One producer may have purchasers for more than his allowable, while others may have allowable production beyond that needed to service their customers. It is therefore necessary to have a free interchange of gas among the producers in the field so that the total market

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[68] Vernon's Civil Stat. of Texas (1925), Art. 6008, §§ 10-20, Art. 6008a, Art. 6049d, §§ 4-13; New Mexico Stat. (1951 Supp.), §§ 69-212, 213, 213½; Oklahoma Stat. Tit. 52, § 239 (1951).

demand for gas can be effectively met. In practice, a producer and gatherer whose allowable production is insufficient to meet his customers' requirements will frequently have to establish connecting lines to purchase from producers who have excess allowable production (R. 382, 470-471, 511-512, 561-562). If the producer and gatherer were under the jurisdiction of the Federal Power Commission, the state efforts in furthering these interconnections would be frustrated by the reluctance or outright refusal of producers to connect with the lines of any one subject to federal regulation because of fear that by doing so they might themselves be subject to federal rate regulation (R. 472-473).

For similar reasons there would be clear interference with state measures to conserve casinghead gas. Thus, the Texas Railroad Commission has found that when it seeks to have flared casinghead gas utilized by having it turned into the line of a company subject to Federal Power Commission regulation, producers strongly resist such efforts because of fear that their sales might be subjected to federal regulation (R. 417-418).

All of these aspects of the state regulatory programs were fully developed in the evidence. On this record, the Commission found that if it attempted to regulate field sales by independent producers and gatherers there would be serious interference with the regulatory programs of the producing states. This conflict might take the form of a direct collision between particular orders, as for example, by a federal rate regulation clashing with a price order such as the one adopted by Oklahoma. Quite apart from such specific conflicts, the exercise of federal jurisdiction over field prices would produce continuing interference, more general but equally direct, with state conservation and related programs. Under federal regulation, standards inherently inconsistent with the state programs and policies would be applicable to the activities and transactions now subject to state authority. The inevitable re-

sult of this inroad by federal authority, however exercised, would be the disruption of the state conservation programs.

This finding was attacked in the court below on a variety of grounds that are all without merit. In part the attacks rested on the assumption that to establish a relevant conflict it was necessary to show a clash between particular price orders. This assumption is erroneous; as the *Interstate* case makes clear the conflict which Congress wished to avoid included any conflict between federal rate regulation and the power of the states "to regulate the physical production and gathering of natural gas". 331 U.S. 682, 690. In part the attacks also rested on the assumption that the states' conservation powers do not permit them to regulate sales such as those made by Phillips, an assumption which, as we have shown, cannot be reconciled with the decision of this Court in the *Cities Service* case. See pages 63-66, *supra*. The Commission's finding was also attacked on the ground that there could be no conflict because federal regulation of the rates of interstate transmission companies had never conflicted with state conservation measures. This contention overlooks the fact that in regulating interstate transmission companies the Federal Power Commission has never directly regulated field sales of natural gas. On the contrary, it has always allowed the interstate transmission companies as an operating expense the full cost of the gas that they purchase from independent producers and gatherers. Since the rate base of interstate transmission companies consists largely of their transmission facilities, public utility regulation of the rates charged by those companies has had only an indirect effect on their producing and gathering activities. See pages 51-56, *supra*.

Nor is there merit in the suggestion made below that federal and state regulation should be applied to the same transactions, or in the same general area of activity, until a direct clash occurs between two incom-

patible orders. The authority of the states over production and gathering cannot be properly administered if it is to turn on the content of, and shifting modifications in, federal regulation. In this sensitive area involving the relationship between federal and state authority, the state regulatory programs cannot be effective if they are constantly subject to nullification by federal regulation.[60] Nothing but the most explicit statutory command could justify an interpretation of the statute that would lead to such results. There is nothing on the face of the Natural Gas Act or in its legislative history that can be used to justify the assertion that the application of the "production or gathering" clause of Section 1(b) is to depend upon day-to-day conflicts between state and federal regulatory authority.

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[60] As this Court observed in Cloverleaf Butter Co. v. Patterson, 315 U.S. 148, 169, "Our duty to deal with contradictory functions of state and nation, . . . calls for the utmost effort to avoid conclusions which interfere with the governmental operations of either. Nothing could be more fertile for discord, however, than a failure to define the boundaries of authority. Clashes may and should be minimized by mutual tolerance; but they are much less likely to happen when each knows of the limits of its responsibility."

See also Bethlehem Steel Co. v. New York State Labor Relations Board, 330 U.S. 767, 775-776:

"But the power to decide a matter can hardly be made dependent on the way it is decided.

* * *

"If the two boards attempt to exercise a concurrent jurisdiction to decide the appropriate unit of representation, action by one necessarily denies the discretion of the other. The second to act either must follow the first, which would make its action useless and vain, or depart from it, which would produce a mischievous conflict. The State argues for a rule that would enable it to act until the federal board had acted in the same case. But we do not think that a case by case test of federal supremacy is permissible here."

The Commission, measuring its regulatory authority and policies against the programs and policies of the producing states, concluded that any federal regulation would by its very nature conflict and seriously interfere with state authority. This factual determination is strong confirmation of the Commission's decision that federal regulation of sales such as those made by Phillips would defeat the intent of Congress.

IV

THE ASSERTION THAT EXTENSION OF FEDERAL REGULATORY POWER TO THE ACTIVITIES OF INDEPENDENT PRODUCERS AND GATHERERS IS REQUIRED TO PROTECT CONSUMERS IS WITHOUT BASIS IN FACT AND IN ANY EVENT RAISES QUESTIONS OF LEGISLATIVE POLICY THAT MAY APPROPRIATELY BE CONSIDERED ONLY BY CONGRESS

Before the Commission and in the court below the advocates of federal regulation relied heavily upon the assertion that regulation of field sales made by independent producers and gatherers is necessary to protect consumers against excessive prices. This assertion has no basis in fact. It was not true in 1938 when the Natural Gas Act was passed and it is not true today that consumers require federal protection against the prices charged by independent producers and gatherers.

Passing for the moment the lack of factual basis for the argument, it should be noted that it is an argument that relies primarily on considerations of alleged economic necessity and public policy. Countervailing considerations of economics and public policy are advanced by those who believe that in the long run the public interest will not be served by fixing field prices for natural gas on a public utility basis. The producing states, for example, assert that federal regulation of field sales will interfere with their conservation programs, will discourage investment, and, in the long range, will injure the economic interest of

both the producing and consuming areas by reducing the supply of gas available for distribution at fair prices.

These conflicting contentions represent a clash between the interests of producing states and the asserted interests of those persons who believe that the field prices of natural gas should be fixed at the lowest levels consistent with the constitutional prohibition against confiscation. The Natural Gas Act does not represent a legislative determination of this conflict. During the deliberations which resulted in the passage of the Act, it was not suggested to Congress that federal regulation of independent producers and gatherers was necessary to protect the interests of consumers. On the contrary, Congress was led to believe that any injury threatened to those interests could be prevented by regulation of the charges levied by the interstate transmission companies for the service they performed in transporting gas from the producing fields to consuming markets. It is for this reason that the legislative history of the Act was marked by no conflict between the producing states and the advocates of federal regulation such as has now arisen. Congress accordingly confined the legislation to the activities of the interstate transmission companies and protected the interests of the consumers by subjecting to federal regulation the charges levied by those companies.

The present conflict between the producing and consuming areas now arises because years after Congress considered the regulatory problem the representatives of some consuming areas assert that they require protection against the field prices charged by independent producers and gatherers. To the extent that they appeal to economic necessity and public policy, they are in effect asking the Commission and the courts to give them regulatory protection which they did not seek from Congress in 1938, which Congress did not then consider, and which Congress has never granted.

The facts presented to Congress at the time that it was considering the passage of the Natural Gas Act showed no

need for federal regulation of field prices charged by independent producers and gatherers. In the course of its investigation the Federal Trade Commission collected information about field prices and its report discusses this information (pp. 128, 198-208). The report points out that in 1934 the average well-head prices per m.c.f. were approximately 3¢ in Oklahoma, 2.2¢ in Texas and 2.7¢ in New Mexico. No suggestion is made in the report that these prices were excessive or that independent producers or gatherers were in a position to charge unreasonable field prices. Nor was there any suggestion in the Committee hearings, in the Committee reports or in the debates on the Natural Gas Act, that field prices were excessive or required federal regulation; as we have seen the attention of Congress was directed to the prices charged by the interstate transmission companies, particularly the prices charged at city gates.

It may be asserted, however, that since the passage of the Natural Gas Act, circumstances have changed and new conditions now make federal regulation of independent producers and gatherers necessary to protect the consumers against excessive rates. This assertion is both untrue in fact and inadmissible as a basis for construing the statute.

This Court, writing in 1950, in *Cities Service Gas Co.* v. *Peerless Oil & Gas Co.*, 340 U. S. 179, 186, and speaking of the Guymon-Hugoton Field, one of the fields involved in this case, pointed out that "the wellhead price of gas is but a fraction of the price paid by domestic consumers at the burner-tip, so that the field price, as herein set, may have little or no effect on the domestic delivered price." The spread between present price levels in the field and in consumer markets is demonstrated by recent Bureau of Mines statistics showing an average value of the well-head of 4.7¢ in New Mexico, 5.4¢ in Oklahoma and 6.2¢ in Texas, as against an average value at points of consumption in Wisconsin of $1.30 for residential use and $1.16 for commercial use, in Michigan of 85¢ for residential use and 77.5¢ for

commercial use, and in Missouri of 69.1¢ for residential use and 48.1¢ for commercial use.[70]

The most recent authoritative general examination of conditions in the gas industry was made in June 1952 by the President's Materials Policy Commission. In its report that body reviewed the price situation in the natural gas industry and pointed out that "natural gas is now selling in many markets, even at greater distances from the principal fields, at a substantially lower price energy wise than competitive fuels for industrial use, and either cheaper or at roughly a competitive price for domestic and commercial uses."[71] Over the period since the passage of the Natural Gas Act, this relative price advantage of natural gas to consumers over other fuels has been increasing rather than decreasing. From the period 1935-1939 to the year 1950, the average retail price of bituminous coal had increased by 91.4%, that of anthracite by 90.1%, that of fuel oils by 90.7% and that of manufactured gas by 9.7%, while over the same period the average price of natural gas to domestic and commercial consumers had declined by 7.0%.[72]

In the instant case the Commission did not attempt to inquire into the reasonableness of the prices charged in the field by independent producers or gatherers nor did it attempt to determine whether Phillips' prices were excessive. Consequently the record does not disclose all the considerations and factors that bear on the reasonableness of the prices now charged in the fields by independent

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[70] Mineral Market Report No. MMS 2229. Mineral Industry Surveys. United States Department of the Interior, Bureau of Mines, November 9, 1953.

[71] Resources for Freedom, Vol. III, The Outlook for Energy Sources, pp. 18-19 (United States Government Printing Office 1952).

[72] Stockton, Henshaw & Graves, Economics of Natural Gas in Texas, Bureau of Business Research, University of Texas (1952), p. 279.

producers and gatherers, including Phillips. There is, however, sufficient evidence in the record to negative any assertion that Phillips' prices are now excessive or exorbitant. The record shows that the prices Phillips charges the interstate transmission companies range from approximately 3¢ per m.c.f. to approximately 8¢ per m.c.f.[73]

Measured against the general change in the price level of all commodities, and taking into account the great increase in demand for natural gas, neither field prices generally, nor Phillips' prices specifically, reflect any substantial change in conditions that requires the exercise of federal regulatory power. But even if it should be assumed, contrary to fact, that some change in market conditions has occurred since the Natural Gas Act was passed, that assumption could serve only to emphasize the more basic point that the proposal to extend federal regulatory authority to the business of independent producers raises numerous and complex questions of legislative policy.[74] These

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[73] In the court below the State of Wisconsin indicated in its brief that for use at its executive residence and at the University of Wisconsin it pays a rate of approximately $1.07 per m.c.f. for gas purchased at 8.17¢ per m.c.f. by Michigan-Wisconsin from Phillips in the field (Brief for Petitioners, State of Wisconsin and Public Service Commission of Wisconsin, in the United States Court of Appeals for the District of Columbia Circuit, No. 11247, pp. 28-29).

[74] For some indication of the complexity and ramifications of the questions involved see, generally, Natural Gas Investigation, Federal Power Commission, Docket No. G-580, Report of Commissioners Smith and Wimberly (United States Government Printing Office 1948); The Outlook for Energy Sources, Vol. III, Resources for Freedom (Paley Report) (United States Government Printing Office 1952); Comment, Federal Price Control of Natural Gas Sold to Interstate Pipelines, 59 Yale L. J. 1468 (1950); Hearings before the Committee on Interstate and Foreign Commerce on H. R. 2185, 80th Cong., 1st Sess. (1947); Hearings before Subcommittee of the Committee on Interstate and Foreign Commerce on S. 734, 80th Cong., 1st Sess. (1947); Hearings before Subcommittee of the Committee on Interstate and Foreign Com-

problems arise both because of the nature of gas as a commodity and because of the nature of the business of producing and gathering.

Gas is a natural resource which is "elusive, exhaustible, and irreplaceable." [75] Once brought to the ground the gas cannot be stored and must be used or sold if it is not to be wasted. It often occurs in the earth in the presence of oil or intermixed with oil and in those circumstances the oil cannot be produced without also producing the gas. Because of these characteristics of gas, the producing states for many years have regulated its production and gathering in the interest of conservation, to prevent waste, and to promote the efficient utilization of this irreplaceable natural resource.

These eccentricities of the commodity are reflected in the characteristics of the business of producing and gathering natural gas. It is essentially a mining or an extractive business and differs in kind from the business of providing transportation services and other similar public utility operations. Success in the business depends upon finding and reducing to possession reserves of natural gas. That in turn depends upon continued capital expenditures for discovery, exploration and development, which are often fruitless. In terms of return on investment the results of these expenditures are therefore erratic, irregular and unpredictable. The ability and willingness of producers to make the expenditures depend upon the prices that they receive for natural gas in the field. The determination of the level of prices necessary to encourage these speculative expenditures for exploration and development raises problems quite different from those involved in fixing a maximum reason-

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merce on H. R. 79, 81st Cong., 1st Sess. (1949); Hearings before Subcommittee of the Committee on Interstate and Foreign Commerce on S. 1498, 81st Cong., 1st Sess. (1949).

[75] Mr. Justice Jackson, dissenting, in Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591, 628, 629.

able return on the rate base of the conventional public utility.[76]

Unlike the interstate transmission business, which even today is in the hands of a comparatively small number of pipe line companies, the business of producing and gathering natural gas is carried on by a large number of separate business units.[77] In 1946 and 1947 approximately 2300 independent producers or gatherers sold gas directly to natural gas companies (R. 728-731). In addition to these 2300 independent producers or gatherers, there are several thousand other independent producers of natural gas who do not sell directly to interstate transmission companies but whose prices affect the prices that the interstate transmission companies pay in the field. Any proposal to reg-

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[76] It has been suggested that in the case of the interstate transmission companies federal rate regulation, even though it has only an indirect impact on producing and gathering properties, has had the effect of discouraging investment for exploration and discovery. See Commissioner Smith concurring in the Matter of Northern Natural Gas Company, Docket No. G-1618, 94 P.U.R. (NS) 485, 507, 511-512 (1952).

There is a marked contrast between the expenditures for exploration and discovery made by independent producers and gatherers such as Phillips and the expenditures made for the same purpose by the integrated transmission companies. In the hearings before the Examiner, Phillips offered to prove the following facts: In 1949 the total exploration expenditures of all thirty-five natural gas companies operating in the southwest amounted to $3,980,000.00. In this year Phillips alone spent $24,700,000.00 in exploration for new gas and oil reserves (Ex. 149; R. 1292-1293). In 1950 Phillips expended $30,300,000.00 in exploration, including leasehold additions to carry on its oil and gas operations (*ibid.*). Included in these exploration expenditures were large sums for drilling exploratory wells, of which some 70 per cent in the past ten years were dry (Ex. 81; R. 349-350, 592-602, 1214). The evidence was excluded.

[77] In 1947 there were 115 natural gas companies subject to regulation by the Federal Power Commission. Statistics of Natural Gas Companies, 1947, p. v.

ulate the field sales of independent producers and gatherers requires consideration of the question whether all of these producers and gatherers should be regulated and if not, where the regulatory line should be drawn.[78]

Because oil rarely occurs without gas, the gas operations of independent producers and gatherers are frequently incidental or ancillary to larger operations in the petroleum industry and the physical facilities that they use in their gas operations are also an integral part of their petroleum business. It would hardly be possible to regulate field prices of natural gas without allocating investment and operating costs as between gas operations and petroleum operations. Even so, the regulation of field prices of natural gas would have a direct and substantial effect upon the oil operations of independent producers or gatherers because, no matter what allocation of investment and cost might be made for accounting purposes, their oil and gas activities are in fact carried on as a unit, and regulation of the return received on one part of the business would necessarily affect the return received on the other.[79]

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[78] It has been estimated that there are approximately 8000 independent producers of natural gas in the United States. See Report of Commissioners Smith and Wimberly, Natural Gas Investigation, Federal Power Commission, Docket No. G-580 (United States Government Printing Office 1948) p. 194. This number presumably includes the 2300 who are known to sell gas directly to interstate transmission companies.

Independent producers who do not sell directly to interstate transmission companies frequently sell to other independent producers or gatherers who do make such sales. The record in this case shows that Phillips buys from other independent producers a substantial part of the gas that it sells to the interstate transmission companies. There is an obvious and direct relationship between the prices Phillips charges the interstate transmission companies and the prices it pays these other independent producers.

[79] The relationship between gas and petroleum operations was recognized by the Commission in its decision in Columbian Fuel Corp., 2 F.P.C. 200 (1940). There the Commission, in disclaim-

The assertion that economic necessity and public policy now require federal regulation of the business of independent producers and gatherers necessarily poses the questions of policy that arise by reason of the facts briefly summarized in the preceding paragraphs. Congress was not attempting to regulate independent producers and gatherers when it passed the Natural Gas Act and therefore it did not have any occasion to consider those questions. Congress did not, for example, consider whether any regulation of sales made in the field by independent producers or gatherers could be effective to protect consumers unless it applied to all sales made by all such producers and gatherers, including those made at the well-head. It did not consider whether the conventional rate-making principles, developed in the regulation of public utility industries whose rate base consisted principally of physical facilities, are appropriate or suitable for application to the business of producing and gathering. There is nothing to indicate that Congress ever considered what effect the application of those standards might have on the willingness of independent producers and gatherers to continue to make expenditures for exploration and development or whether the application of those standards might adversely affect the supply of gas available to consumers. Congress did not attempt to weigh the short-term advantage of the small reductions in the consumer price that might be achieved by regulation of field prices against the long-range interest of the consumer in an adequate and

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ing authority to regulate sales made in the field by independent producers and gatherers, emphasized that assuming such jurisdiction

> "would lead the Commission into attempts to deal with the complicated interrelationship between the natural-gas industry and the oil industry. To make regulation of producers and gatherers effective under these circumstances would require statutory authority of much wider scope. . . ." (2 F.P.C. at 207)

assured supply of gas. Nor did Congress consider the regulatory problems that arise by reason of the fact that any regulation of field sales of natural gas must necessarily have a direct impact on the petroleum business of independent producers and gatherers.

Viewed in this light, arguments based on alleged economic necessity and public policy provide no basis for rejecting the construction of the statute followed by the Federal Power Commission in this case. On the contrary, the fact that Congress never considered the questions of legislative policy that those arguments raise supplies additional and substantial support for the conclusion that Congress never intended the Natural Gas Act to apply to the business of independent producers and gatherers.

CONCLUSION

For all the foregoing reasons the judgment of the Court of Appeals should be reversed.

Respectfully submitted,

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APPENDIX A

Pertinent Provisions of Statute

NATURAL GAS ACT OF JUNE 21, 1938, 52 STAT. 821-833; AS AMENDED FEBRUARY 7, 1942, 61 STAT. 459

Section 1. (a) As disclosed in reports of the Federal Trade Commission made pursuant to Senate Resolution 83 (Seventieth Congress, first session) and other reports made pursuant to the authority of Congress, it is hereby declared that the business of transporting and selling natural gas for ultimate distribution to the public is affected with a public interest, and that Federal regulation in matters relating to the transportation of natural gas and the sale thereof in interstate and foreign commerce is necessary in the public interest.

(b) The provisions of this act shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural-gas companies engaged in such transportation or sale, but shall not apply to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural gas [52 Stat. 821 (1938); 15 U. S. C. § 717 (1946)]

Sec. 2. When used in this act, unless the context otherwise requires—

* * *

(6) "Natural-gas company" means a person engaged in the transportation of natural gas in interstate commerce, or the sale in interstate commerce of such gas for resale.

* * *

Sec. 4. (a) All rates and charges made, demanded, or received by any natural-gas company for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges, shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) No natural-gas company shall, with respect to any transportation or sale of natural gas subject to the juris-

diction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Under such rules and regulations as the Commission may prescribe, every natural-gas company shall file with the Commission, within such time (not less than sixty days from the date this act takes effect) and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection, schedules showng all rates and charges for any transportation or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Unless the Commission otherwise orders, no change shall be made by any natural-gas company in any such rate, charge, classification, or service, or in any rule, regulations, or contract relating thereto, except after thirty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the thirty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Whenever any such new schedule is filed the Commission shall have authority, either upon complaint of any State, municipality, or State commission, or upon its own initiative without complaint, at once, and if it so orders, without answer or formal pleading by the natural-gas company, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules

and delivering to the natural-gas company affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect: *Provided,* That the Commission shall not have authority to suspend the rate, charge, classification, or service for the sale of natural gas for resale for industrial use only; and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of the suspension period, on motion of the natural-gas company making the filing, the proposed change of rate, charge, classification, or service shall go into effect. Where increased rates or charges are thus made effective, the Commission may, by order, require the natural-gas company to furnish a bond, to be approved by the Commission, to refund any amounts ordered by the Commission, to keep accurate accounts in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts were paid, and, upon completion of the hearing and decision, to order such natural-gas company to refund, with interest, the portion of such increased rates or charges by its decision found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the natural-gas company, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible. [52 Stat. 822 (1938); 15 U. S. C. 717c (1946)]

* * *

SEC. 5. (a) Whenever the Commission, after a hearing had upon its own motion or upon complaint of any State, municipality, State commission, or gas distributing company shall find that any rate, charge or classification demanded, observed, charged, or collected by any natural-gas company in connection with any transportation or sale of natural gas, subject to the jurisdiction of the Commission,

or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order: *Provided, however,* That the Commission shall have no power to order any increase in any rate contained in the currently effective schedule of such natural gas company on file with the Commission, unless such increase is in accordance with a new schedule filed by such natural gas company; but the Commission may order a decrease where existing rates are unjust, unduly discriminatory, preferential, otherwise unlawful, or are not the lowest reasonable rates.

(b) The Commission upon its own motion, or upon the request of any State commission, whenever it can do so without prejudice to the efficient and proper conduct of its affairs, may investigate and determine the cost of the production or transportation of natural gas by a natural-gas company in cases where the Commission has no authority to establish a rate governing the transportation or sale of such natural gas. [52 Stat. 823 (1938); 15 U. S. C. 717d (1946)]

* * *

SEC. 7. (a) Whenever the Commission, after notice and opportunity for hearing, finds such action necessary or desirable in the public interest, it may by order direct a natural-gas company to extend or improve its transportation facilities, to establish physical connection of its transportation facilities with the facilities of, and sell natural gas to, any person or municipality engaged or legally authorized to engage in the local distribution of natural or artificial gas to the public, and for such purpose to extend its transportation facilities to communities immediately adjacent to such facilities or to territory served by such natural-gas company, if the Commission finds that no undue burden will be placed upon such natural-gas company thereby: *Provided,* That the Commission shall have no authority to compel the enlargement of transportation facilities for such purposes, or to compel such natural-gas company to establish physical connection or sell natural

gas when to do so would impair its ability to render adequate service to its customers. [52 Stat. 824 (1938); 15 U. S. C. 717f (a) (1946)]

(b) No natural-gas company shall abandon all or any portion of its facilities subject to the jurisdiction of the Commission, or any service rendered by means of such facilities, without the permission and approval of the Commission first had and obtained, after due hearing, and a finding by the Commission that the available supply of natural gas is depleted to the extent that the continuance of service is unwarranted, or that the present or future public convenience or necessity permit such abandonment. [52 Stat. 824 (1938); 15 U. S. C. 717f (b) (1946)]

(c)[1] No natural-gas company or person which will be a natural-gas company upon completion of any proposed construction or extension shall engage in the transportation or sale of natural gas, subject to the jurisdiction of the Commission, or undertake the construction or extension of any facilities therefor, or acquire or operate any such facilities or extensions thereof, unless there is in force with respect to such natural-gas company a certificate of public convenience and necessity issued by the Commission authorizing such acts or operations: *Provided, however.* That if any such natural-gas company or predecessor in interest was bona fide engaged in transportation or sale of natural gas, subject to the jurisdiction of the Commission, on the effective date of this amendatory Act, over the route or routes or within the area for which application is made and has so operated since that time, the Commission shall issue such certificate without requiring further proof that public convenience and necessity will be served by such operation, and without further proceedings, if application for such certificate is made to the Commission within ninety days after the effective date of this amendatory Act. Pending the determination of any such application, the continuance of such operation shall be lawful.

In all other cases the Commission shall set the matter for hearing and shall give such reasonable notice of the hearing thereon to all interested persons as in its judgment may be necessary under rules and regulations to be prescribed by

[1] Subsection 7 (c) was amended February 7, 1942 by Public Law No. 444, 77th Congress, Chapter 49, 2d Session [H. R. 5249], 56 Stat. 83.

the Commission; and the application shall be decided in accordance with the procedure provided in subsection (e) of this section and such certificate shall be issued or denied accordingly: *Provided, however,* That the Commission may issue a temporary certificate in cases of emergency, to assure maintenance of adequate service or to serve particular customers, without notice of hearing, pending the determination of an application for a certificate, and may by regulation exempt from the requirements of this section temporary acts or operations for which the issuance of a certificate will not be required in the public interest. [52 Stat. 825 (1938), as amended, 56 Stat. 83 (1942); 15 U. S. C. § 717f (c) (1946)].[2]

* * *

SEC. 11 (a) In case two or more States propose to the Congress compacts dealing with the conservation, production, transportation, or distribution of natural gas it shall be the duty of the Commission to assemble pertinent information relative to the matters covered in any such proposed compact, to make public and to report to the Congress information so obtained, together with such recommendations for further legislation as may appear to be ap-

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[2] As originally enacted June 21, 1938 by Public Law No. 688, 75th Congress, Chapter 556, 3d Session [H. R. 6586], 52 Stat. 825, Section 7 (c) read as follows:

"(c) No natural-gas company shall undertake the construction or extension of any facilities for the transportation of natural gas to a market in which natural gas is already being served by another natural-gas company, or acquire or operate any such facilities or extensions thereof, or engage in transportation by means of any new or additional facilities, or sell natural gas in any such market, unless and until there shall first have been obtained from the Commission a certificate that the present or future public convenience and necessity require or will require such new construction or operation of any such facilities or extensions thereof: *Provided, however,* That a natural-gas company already serving a market may enlarge or extend its facilities for the purpose of supplying increased market demands in the territory in which it operates. Whenever any natural-gas company shall make application for a certificate of convenience and necessity under the provisions of this subsection, the Commission shall set the matter for hearing and shall give such reasonable notice of the hearing thereon to all interested persons as in its judgment may be necessary under rules and regulations to be prescribed by the Commission. In passing on applications for certificates of convenience and necessity, the Commission shall give due consideration to the applicant's ability to render and maintain adequate service at rates lower than those prevailing in the territory to be served, it being the intention of Congress that natural gas shall be sold in interstate commerce for resale for ultimate public consumption for domestic, commercial, industrial, or any other use at the lowest possible reasonable rate consistent with the maintenance of adequate service in the public interest." (52 Stat. 825 (1938))

propriate or necessary to carry out the purposes of such proposed compact and to aid in the conservation of natural-gas resources within the United States and in the orderly, equitable, and economic production, transportation, and distribution of natural gas.

(b) It shall be the duty of the Commission to assemble and keep current pertinent information relative to the effect and operation of any compact between two or more States heretofore or hereafter approved by the Congress, to make such information public, and to report to the Congress, from time to time, the information so obtained together with such recommendations as may appear to be appropriate or necessary to promote the purposes of such compact.

(c) In carrying out the purposes of this act, the Commission shall, so far as practicable, avail itself of the services, records, reports, and information of the executive departments and other agencies of the Government, and the President may, from time to time, direct that such services and facilities be made available to the Commission. [52 Stat. 827 (1938); 15 U. S. C. 717j (1946)]

* * *

SEC. 19 * * *

(b) Any party to a proceeding under this act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the circuit court of appeals of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall forthwith be served upon any member of the Commission and thereupon the Commission shall certify and file with the court a transcript of the record upon which the order complained of was entered. Upon the filing of such transcript such court shall have exclusive jurisdiction to affirm, modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court un-

less such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If any party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceedings before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings, which if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court, affirming, modifying, or setting aside, in whole or in part, any such order of the Commission, shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in sections 239 and 240 of the Judicial Code, as amended (U. S. C., title 28, secs. 346 and 347).

* * *

GOLDSMITH SYSTEM
TRANSMISSION LINES OF RESIDUE PURCHASERS
GATHERING LINES
RESIDUE LINES
FIELD BOOSTERS
SID RICHARDSON

Appendix B